



Epwin Holdings Limited/Latium Building Products Holdings Limited, CET Glass Processors Holdings Limited and Building Plastics Holdings Limited merger inquiry

A report on the completed acquisition by Epwin Holdings Limited of Latium Building Products Holdings Limited, CET Glass Processors Holdings Limited and Building Plastics Holdings Limited

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The Competition Commission has excluded from this published version of the final report information which the inquiry group considers should be excluded having regard to the three considerations set out in section 244 of the Enterprise Act 2002 (specified information: considerations relevant to disclosure). The omissions are indicated by [X]. Some numbers have been replaced by a range. These are shown in square brackets. Non-sensitive wording is also indicated in square brackets.

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Glossary

Summary

1. On 18 June 2012, the Office of Fair Trading (OFT) referred the completed acquisition by Epwin (Holdings) Limited (Epwin) of Latium Building Products Holdings Limited (Latium) to the Competition Commission (CC) for investigation and report.
2. The OFT varied the reference on 16 July 2012 to include the acquisition by Epwin of Building Plastics Holdings Limited (Building Plastics) and CET Glass Processors Holdings Limited (CET). The acquisition of Building Plastics and CET took place at the same time, and as part of the same transaction, as Epwin's acquisition of Latium.
3. Our provisional findings were published on 8 October 2012. We were required to publish our final report by 2 December 2012.
4. Epwin acquired Latium, Building Plastics and CET on 16 January 2012. The companies involved in the acquisition are variously engaged in the manufacture and supply of a wide range of PVC building products. Our inquiry concentrated on the parties' horizontal overlap in the manufacture and supply of PVC-extruded flat boards and trims which are fitted around the roofline (roofline products) and windows (window trims) of houses.
5. PVC roofline and window-trim products are used in the construction of new houses and the refurbishment of existing properties. Refurbishments range from small-scale refurbishments of individual houses by local builders and roofers to large-scale refurbishments of social housing stock by major contractors. The products are generally distributed through stockists, some of which are owned by manufacturers. The stockists take delivery of the products from manufacturers and sell them either directly to end-users or to other smaller sub-stockists. The end-users of PVC roofline and window-trim products are builders, roofers and other tradesmen who install them on houses.
6. We concluded that the turnover test and the share of supply were met and that a relevant merger situation had been created.
7. We concluded that the appropriate market definition was the supply of PVC roofline and window-trim products in the UK.
8. We considered the situation that would have prevailed absent the acquisition (the counterfactual). We concluded that, in the absence of the merger with Epwin, Latium would most likely have been sold to a third party either by a process of negotiation or through administration. The purchaser would most likely have been a company involved in the extrusion of PVC building products.
9. We assessed the extent of pre-merger competition in the market for the supply of PVC roofline and window-trim products. We identified two customer segments. Smaller end-users, such as local builders and roofers, buy PVC roofline and window-trim products directly from a stockist, over the 'trade counter', without any interaction with the manufacturer (the trade segment). Larger end-users, such as national house builders and social housing contractors, generally have an agreement with a manufacturer which supplies PVC roofline and window-trim products of a particular specification through stockists (the specification segment).
10. We noted that, for both customer segments, interactions for the purchase of PVC roofline and window-trim products are characterized by frequent bilateral negotiations. We refer to this as a bargaining framework. We examined three factors which

would affect the alternative options of buyers within this framework and assessed them in the context of the UK PVC roofline and window-trim market.

11. First, we assessed the extent to which products in the market were differentiated between different manufacturers and brands. Our view was that the products are relatively homogenous. Second, we considered the extent of any switching costs that might make it difficult for stockists or end-users to change supplier. We considered that switching costs were not a sufficiently high barrier to prevent stockists from changing supplier and that there were no material switching costs for end-users. Third, we assessed whether and to what extent alternative suppliers had spare capacity to produce roofline products and window-trim products in response to an increase in demand. Our analysis indicated, based on conservative assumptions, that the parties' competitors had around 13,000 tonnes of spare capacity between them.
12. We considered the implications post-merger of our spare capacity estimates for the two customer segments we had identified. We considered that customers in both segments of the market had the ability to negotiate.
13. In assessing the potential merger effect on the specification segment, we considered that between them, competitors to the parties in this segment had sufficient spare capacity such that they could serve all top ten national house builders, were they to switch away from Epwin/Latium. Therefore, in our view, customers in the specification segment would have viable alternative options to the merged parties which would constrain the merged parties' ability to increase prices or reduce quality or choice to this segment.
14. In relation to the trade segment, we noted that, based on our estimates of spare capacity, smaller independent stockists buying relatively low volumes would have a number of alternative suppliers with spare capacity post-merger. We considered separately the merger effect on larger chains of stockists and our view was that the largest stockist chain would potentially be able to switch supply for all of its trade customers from the merged parties. The ability to threaten to switch supply would constrain the merged parties' ability to increase prices or reduce quality or choice to this segment.
15. We noted that our estimate of the spare capacity of the merged parties' competitors would not be sufficient to meet demand in the unlikely scenario that all of Epwin/Latium's customers across both segments wanted to change supplier simultaneously. However, we noted that in a bargaining framework, prices are constrained by a customer's ability to negotiate and to have a viable alternative option as the basis for the negotiation. Not all customers of the merged parties would need to change supplier; they would only need to have a viable alternative option to the merged parties to which they could threaten to switch in negotiations. We considered that our estimate of spare capacity was such that there would be sufficient alternative options across both customer segments to constrain the merged parties.
16. We also assessed the availability of swing capacity. Swing capacity is the potential for existing manufacturers of roofline and window-trim products to expand their production by reallocating production lines currently used to produce other PVC extruded products outside the market, such as rainwater products. Our view was that swing capacity available to manufacturers within the market may be expected to act as a further competitive constraint on the parties.
17. We considered new entry by companies manufacturing other PVC products and expansion by existing competitors. The evidence we received suggested that there

was little immediate prospect of significant entry into the UK market by companies producing related PVC products or for expansion by those already in the market because the market conditions were not favourable.

18. The evidence suggested that expansion by an existing PVC extruder, with access to raw materials at competitive prices, could be achieved for a relatively modest investment in time and money and also that there was potential for increased imports if exchange rates were favourable. We noted that either of these could provide a constraint on the merged entity if market conditions changed. We further noted a general consensus that the barriers appeared high for a party to enter the PVC roofline and window-trim market from outside the PVC extrusion industry.
19. We also considered three other potential effects of the merger. First, we considered the potential for the merged parties to use the multiple brands available to them post-merger to offer geographic exclusivity to independent stockists to the detriment of other manufacturers with fewer or single brands. We considered that the merger of two companies with multiple brands did not raise competition concerns.
20. Second, we assessed the potential ability of the merged parties to entice a stockist to switch to them from a competitor by offering new business from the specification sector. Our view was that the merger was unlikely to result in the merged parties having the ability to encourage stockists to switch supplier in return for increased sales to specification customers.
21. Third, we considered whether the merged parties could threaten to withdraw a brand or product from independent stockists in favour of their own outlets if the stockist did not accept margin arrangements agreed with end-users in the specification segment. We considered that it was not likely that the merged parties would be able to fore-close independent stockists.
22. Overall, based on our assessment of the competitive effects of the merger, we concluded that the merger has not resulted, and may not be expected to result, in a substantial lessening of competition within any market or markets in the UK for goods or services.

Findings

1. The reference

- 1.1 On 18 June 2012, the OFT referred the completed acquisition by Epwin of Latium to the CC for investigation and report.
- 1.2 The OFT varied the reference on 16 July 2012 to include the acquisition by Epwin of Building Plastics and CET. The acquisition of Building Plastics and CET had taken place at the same time, and as part of the same transaction, as Epwin's acquisition of Latium.
- 1.3 The CC must decide:
 - (a) whether a relevant merger situation has been created; and
 - (b) if so, whether the creation of that situation has resulted, or may be expected to result, in a substantial lessening of competition (SLC) within any market or markets in the UK for goods or services.
- 1.4 Our terms of reference are in Appendix A. We were required to take our final decision by 2 December 2012.
- 1.5 This document, together with its appendices, constitutes our final report, which we are required to publish under section 38(1) of the Enterprise Act 2002 (the Act). Further information, including non-commercially-sensitive versions of the submission from Epwin and Latium, summaries of evidence from third parties, the survey of installers and stockists commissioned by the CC, and our provisional findings published on 8 October 2012, can be found on our website.

2. The production and distribution of PVC-extruded building products

- 2.1 The companies involved in the acquisition are variously engaged in the manufacture and supply of PVC building products. This section briefly describes the use of PVC-extruded products in the construction and refurbishment of buildings. Section 3 describes the various companies brought together by the acquisition.

History of the industry

- 2.2 The large-scale production of PVC-extruded building products dates back to the 1970s when the first PVC window systems were made and installed.¹ PVC-extrusion techniques subsequently began to be used for a wider range of products such as guttering and drainpipes (rainwater), and boards under the eaves of houses (roofline). The industry expanded very quickly in the 1980s and 1990s as PVC was marketed, as it continues to be, as a maintenance-free replacement for traditional materials, such as metal for rainwater and timber for roofline.

¹ See *Plastics in construction: a guide for architects and specifiers*, the British Plastics Federation (BPF) and other information on the BPF website: www.bpf.co.uk.

Products

2.3 PVC is used to manufacture a range of building products including high-specification door and window systems, and rainwater products, such as down pipes and guttering. PVC is extruded to make a wide variety of flat boards and trims, traditionally made of wood, which are fitted around the roofline and windows of houses. These products include:

- fascias—flat boards that sit underneath the eaves of a house, fitted to the roof's overhang;
- soffit boards—flat boards that sit underneath the eaves of a house, perpendicular to the wall;
- PVC cladding—cladding that is attached to the walls of a house; and
- window trims—narrow boards that surround installed windows to provide a finish that matches the window system.

2.4 It is these products which are the main focus of our inquiry (see paragraph 5.3 below).

2.5 Figure 1 illustrates the different types of PVC products used in house building and refurbishment.

FIGURE 1

PVC building products



Source: Epwin.

Production process

- 2.6 PVC extrusion involves melting plastic raw materials and forcing the melted plastic through extruders which can be adjusted according to the final profile and shape of the plastic product required.
- 2.7 Roofline and window-trim products are usually cellular products; that is, they are manufactured with a honeycomb structure and have some of the same properties as timber.² Some, generally considered to be of inferior quality,³ may be hollow and rigid in construction, such as hollow soffit boards. Rainwater products are rigid in construction.
- 2.8 While the extruders used to make different building products are essentially the same, different tooling is required to produce profiles of different shapes and downstream equipment, such as packing machines, may also vary according to the product being extruded. Appendix B describes the extrusion process in more detail.

Distribution

- 2.9 The end-products are generally distributed through stockists.⁴ Stockists take delivery of PVC roofline and window-trim products from manufacturers and sell them on, either directly to end-users, or to other, smaller sub-stockists.
- 2.10 Most stockists are independent businesses; however, a small proportion are part of the same vertically-integrated business.⁵ Stockists include large specialist sellers of PVC building products, such as SIG Roofline; national builders' merchants,⁶ such as Jewson and Travis Perkins which sell a wide range of products to the construction industry; and smaller stockists typically operating out of small units, such as those on trading estates. Roofline and window-trim products may also be sold through window suppliers. In the survey commissioned by the CC for this inquiry,⁷ we categorized stockists into five groups: plastics suppliers; builders' merchants; window suppliers; roofers' merchants; and roofing product specialists (see Figure 2 in paragraph 2.14).

End-users

- 2.11 The end-users of PVC roofline and window-trim products are generally builders, roofers, installers and other tradesmen who fit them to houses. They can range from a sole-trader roofer to a large regional or national house builder. A window installer may also install roofline and window-trim products as part of a wider refurbishment or new-build project. In our survey, we categorized end-users into five groups: window

² Joints and corners are produced by injection moulding.

³ Installers suggest that the hollow nature of the product means it can be prone to brittleness. See, for example, www.squaredealupvc.co.uk/FAQ.asp and <http://www.windowwise.co.uk/advertising/roofline.pdf>.

⁴ We were told of only one example of where a manufacturer sold PVC roofline products directly to a customer rather than through a stockist.

⁵ We were told that there are around 200 manufacturer-owned stockists. The OFT estimated the number of independent outlets for PVC roofline at around 4,000–5,000.

⁶ Our comparison of turnover for PVC roofline and window trim products between different types of stockist suggests that the total volumes distributed by builders' merchants are lower than those of specialist plastics distributors. For example, Jewson and Travis Perkins each have less than 10 per cent of SIG Roofline's UK turnover for PVC roofline products. We were told that this was because of the large amount of shelf space taken up by roofline products and that it needed careful handling and storage.

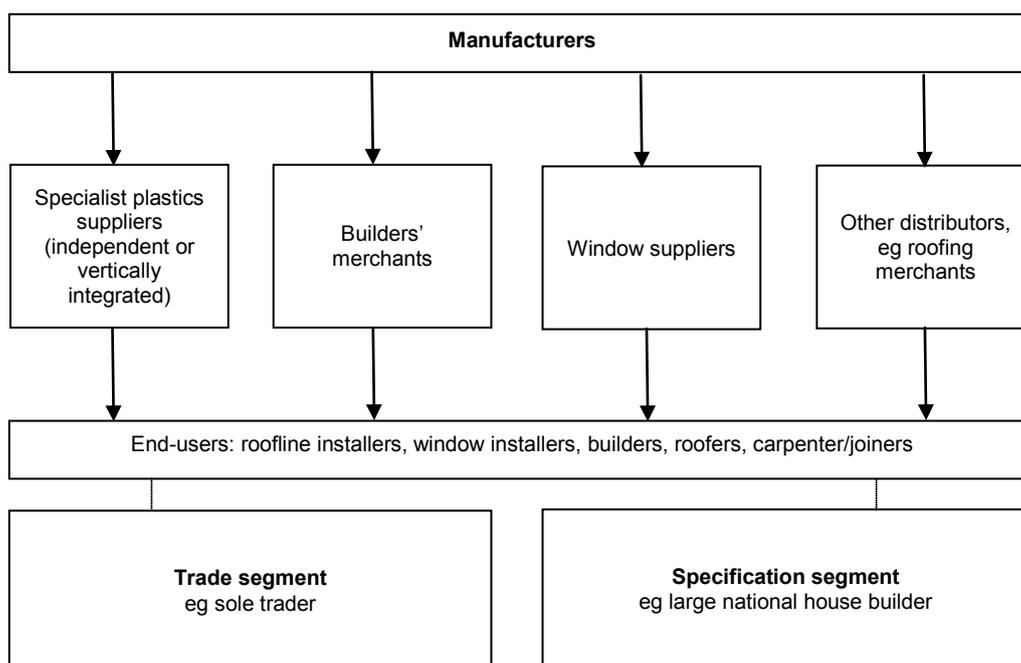
⁷ The CC commissioned DJS Research Ltd to carry out a survey of Epwin/Latium stockists and installers of PVC roofline. The results are available on our website: www.competition-commission.org.uk/our-work/epwin-latium/evidence/cc-commissioned-research-and-surveys.

installers; roofers; specialist roofline installers; builders; and carpenter/joiners. Customers may also come from the DIY sector.

- 2.12 PVC roofline and window-trim products are used in the refurbishment of existing properties and in the construction of new houses. The parties estimated that new-build represented approximately 10 to 15 per cent of the total supply of PVC roofline and window-trim products, with refurbishments constituting the remainder. Refurbishments range from small-scale refurbishments of individual houses by small contractors to large-scale refurbishments of social housing stock by major contractors.
- 2.13 In general, smaller end-users buy PVC roofline and window-trim products directly from a stockist, over the 'trade counter', without any interaction with the manufacturer. In the remainder of this report we refer to this as the trade segment. By contrast, larger end-users, such as house builders and contractors undertaking refurbishments for social housing providers,⁸ will generally have an agreement with a manufacturer which supplies PVC roofline and window-trim products of a particular specification through stockists. We subsequently refer to this as the specification segment.
- 2.14 Figure 2 shows the relationships between manufacturers, stockists and end-users.

FIGURE 2

Supply chain for PVC roofline and window-trim products



Source: CC based on submissions from main and third parties.

- 2.15 How prices are set for the trade and specification segments and differences in the relationship between independent stockists and vertically-integrated stockists and manufacturers are discussed in further detail in Section 7.

⁸ The parties estimated that new build accounted for 10–15 per cent of the market and social housing refurbishment represented approximately a further 10 per cent.

3. The companies

- 3.1 On 16 January 2012, Epwin acquired Latium, Building Plastics and CET through a 'share for share' exchange. In the following section we set out a brief history and description of the relevant businesses which prior to the acquisition were principally owned by two individuals: Mr Jim Rawson (Epwin) and Mr Brian Kennedy (Latium, Building Plastics and CET). In Section 4, we describe the merger situation and the rationale for it.

Epwin

- 3.2 Epwin was one of the first manufacturers of PVC window frames in the UK. The business grew both organically and by acquisition and in 1987 its shares were listed on the Unlisted Securities Market. It transferred to the Official List of the London Stock Exchange in 1992 but was taken private again in 1999, under the control of Mr Rawson. At around the same time Epwin acquired the Swish Building Products business (Swish).
- 3.3 Epwin told us that its business now consisted of the manufacture of extruded PVC window profiles; toughened glass and sealed units for third party or internal use in window and door manufacture; cellular PVC and rigid PVC products and associated mouldings mainly for roofline, window-trim and rainwater uses; and window frames, doors and conservatories. Epwin also owned the largest PVC recycling and re-processing business in the UK and a chain of building product stockists and window sales outlets.
- 3.4 On 19 October 2011, the business was restructured and split into a property investment business and a trading business each controlled independently by Mr Rawson. Epwin Group Limited (Epwin Group), which had previously been the overall holding company, retained the Group's property interests; Epwin, a new holding company, became the parent company of the two trading subsidiaries, SBP Limited (SBP), the manufacturing arm, and Venture Plastics Ltd (Venture Plastics), the distribution arm.
- 3.5 Epwin, via its subsidiary SBP, operates through three divisions: the Extruded Windows Division; the Building Products Division; and the Extruded Building Components Division. The Extruded Building Components division manufactures roofline, window-trim, rainwater and other PVC building products mainly at the Swish plant in Tamworth but also at a plant in Birmingham. Swish sells products under a variety of brand names as well as its own, including Concord, Summit and Plaslyne.
- 3.6 Epwin owns 27 specialist plastics stockists which trade as: Quay Plastics (16 branches mainly in the Midlands and the North of England); Venture Building Plastics (five branches in the Midlands); and Shepherds, acquired on 19 January 2012 (six branches in the South-East). Swish also supplies the Building Products Division's Window Store chain of 16 branches in the South-West. The Window Store chain primarily focuses on the sale of finished windows but also sells some roofline, window-trim and rainwater products. Swish also manufactures own-label brands on behalf of a number of its customers.

Latium, Building Plastics and CET

- 3.7 The companies acquired by Epwin (Latium, Building Plastics and CET) were acquired by Mr Kennedy in August 2005. Through his company Latium Plastics Holdings Limited, now renamed Building Plastics, Mr Kennedy acquired HW Plastics Ltd (HW Plastics) from Heywood Williams plc. Figure 3 below illustrates the structure

of the various companies acquired by Epwin and includes companies which evolved from the acquisition of HW Plastics and are described briefly below.

- 3.8 At the time of the acquisition of HW Plastics, it comprised three trading divisions. Following the acquisition, and subsequent corporate restructures, these divisions became three trading companies: Spectus Systems Limited (Spectus), a window systems manufacturer, and Trentham Logistics Limited (Trentham), a logistics company, both owned by Building Plastics; and Kestrel-BCE Ltd (Kestrel), a manufacturer of PVC building products, owned by Latium.
- 3.9 HW Plastics remains as a non-trading subsidiary of Building Plastics. It holds the lease for a warehouse at Trentham Lakes, Stoke-on-Trent, which it subleases to Trentham and from which Trentham supplies logistics services to Spectus and Kestrel.
- 3.10 Latium subsequently merged Celuform Building Products Limited (Celuform) with Kestrel. Celuform's business, the extrusion of PVC building products, was relocated from Kent to Scunthorpe within the factory leased by Kestrel. Latium continues to produce PVC roofing products at its Scunthorpe plant under three brand names: Kestrel, BCE and Celuform.
- 3.11 Indigo Products Limited (Indigo), a business which made window frames and was previously part-owned by Mr Kennedy, was acquired by Latium on 16 January 2012, the same day as the acquisition by Epwin of Latium. CET manufactures a wide range of glass and glass sealed units for supply to Indigo, to other companies owned by Mr Kennedy, and to third party window and door manufacturers.

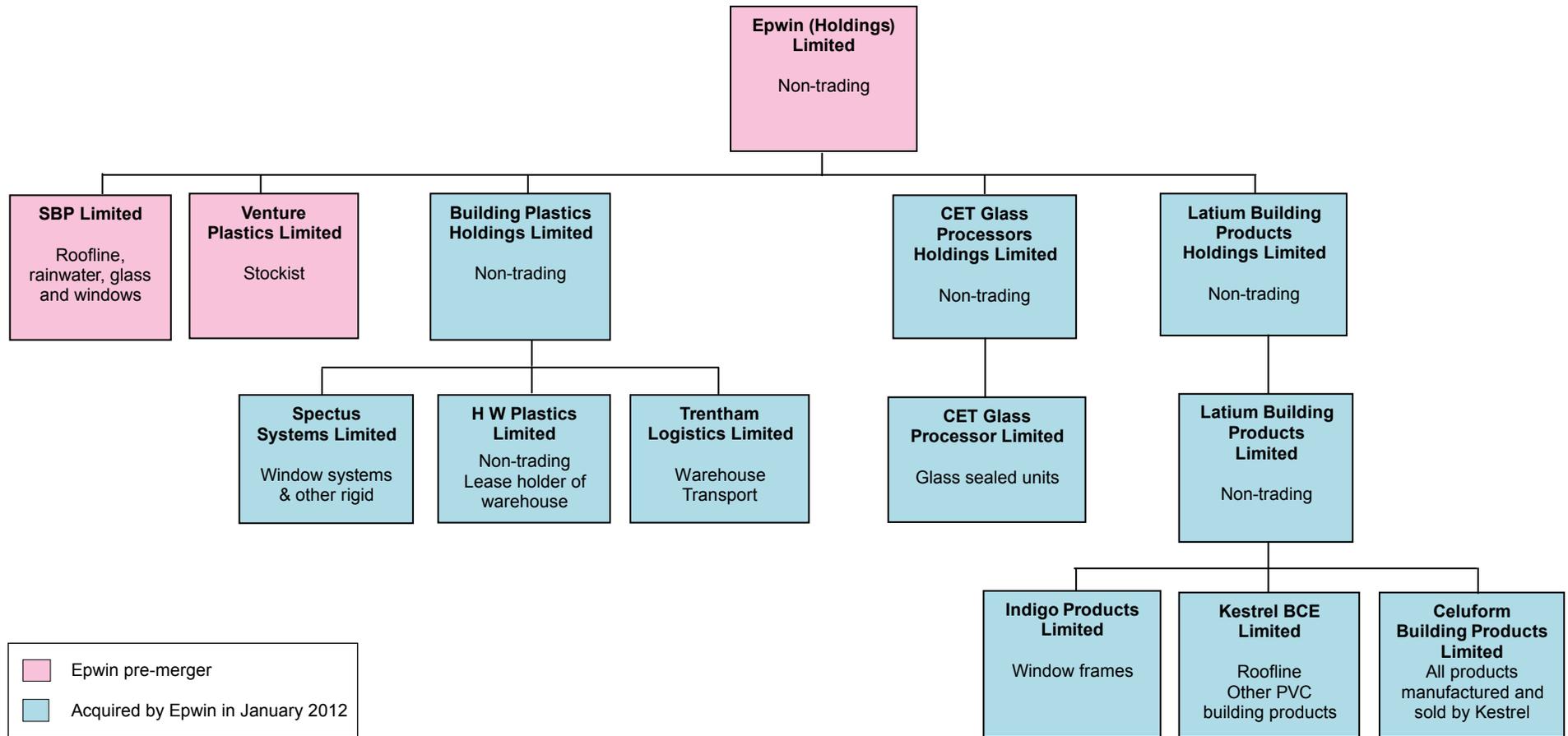
4. The completed merger and the relevant merger situation

Outline of merger situation

- 4.1 The proportion of shares assigned to each shareholder in the transaction was calculated so as to reflect the relative profitability of the businesses being merged, [REDACTED]. The parties told us that [REDACTED]. Following the merger, Mr Rawson owns 53 per cent of the merged businesses and Mr Kennedy 44 per cent. The remaining 3 per cent of shares are owned by other parties who had minority interests in the merging companies.
- 4.2 The completed acquisition brought together a number of businesses engaged in the manufacture or distribution of PVC window and building products for use in new and refurbished buildings. Figure 3 below sets out the structure of the companies brought together under Epwin on the completion of the transaction.

FIGURE 3

Epwin Holdings Ltd statutory corporate structure post-merger



Source: Epwin.

The rationale for the merger

- 4.3 Epwin told us that underlying the rationale for the merger was a change in the market for PVC building products. [REDACTED] Epwin also said that PVC building components was a relatively young industry, which had expanded very quickly in the 1980s and 1990s. The demand for PVC as a maintenance-free replacement for timber had inevitably waned after the initial take-up and the long life of the PVC product meant that there was generally no need to replace it for 20 or 30 years.
- 4.4 Epwin told us that these events had resulted in overcapacity in the industry. At the same time, manufacturers had little control over the price of PVC resin, the main raw material input, because it was highly influenced by the price of oil which had been increasing in recent years. PVC and other raw materials typically make up around [50–60] per cent of the selling price of PVC roofline and window-trim products. Epwin said that [REDACTED].
- 4.5 The parties told us that the owners foresaw that, if the various businesses were combined, opportunities would arise to reduce the costs of manufacture and improve manufacturing capabilities; [REDACTED].
- 4.6 Latium told us that there was an additional [REDACTED] aspect to the transaction. [REDACTED]
- 4.7 Furthermore, Latium told us [REDACTED].⁹

Jurisdiction

- 4.8 Under section 35(1) of the Act, the CC is required to decide whether a relevant merger situation has been created such that:
- (a) two or more enterprises have ceased to be distinct; and
 - (b) either the UK turnover test or the UK share of supply test is satisfied.
- 4.9 An ‘enterprise’ is defined by section 129(1) of the Act as the activities, or part of the activities, of a business and the definition of ‘business’ includes any ‘undertaking which is carried on for gain or reward or which is an undertaking in the course of which goods or services are supplied otherwise than free of charge’.
- 4.10 Epwin, Building Plastics, CET and Latium are active in the manufacture and supply of either window systems or window frames, or glass sealed units, or roofline products, and accordingly we are satisfied that they are enterprises for the purposes of section 129(1) of the Act. As described in paragraph 3.1 above, Epwin acquired the entire issued share capital of Latium, Building Plastics and CET on 16 January 2012 and consequently the enterprises have ceased to be distinct.
- 4.11 Under section 23 of the Act, the UK turnover test is met where the value of the turnover in the UK of the ‘enterprise being taken over’ exceeds £70 million. The UK turnover in the year ended 31 December 2011 of the businesses acquired by Epwin exceeds £70 million excluding inter-company turnover and exports. Therefore, we conclude that the UK turnover test is satisfied.

⁹ [REDACTED]

- 4.12 Under section 23 of the Act, the share of supply test is met if, as a result of the acquisition, the merged enterprises will collectively supply or acquire 25 per cent or more of goods or services of a particular description in the UK or in a substantial part of it. As our Merger Assessment Guidelines (the Guidelines) explain, the share of supply test is different from a market share and goods or services to which the share of supply test is applied need not amount to the market defined for the economic analysis.¹⁰
- 4.13 Epwin and Latium estimate that Epwin ([20–30] per cent) and Latium ([10–20] per cent) together account for a total of [30–50] per cent of the supply by volume of PVC roofline products in the UK and Republic of Ireland in 2011. They stated that they could not reliably estimate their 2011 shares of supply for the UK only but had no reason to believe that their share in the UK only would be materially different from their share of supply in the UK and the Republic of Ireland together. Based on these submissions, we conclude that the UK share of supply test is satisfied.
- 4.14 Therefore, we conclude that the acquisition by Epwin of Latium, Building Plastics and CET has resulted in a relevant merger situation.

5. Market definition

Horizontal overlap

- 5.1 Epwin, Latium, Building Plastics and CET overlap across the various trading companies in the supply of:
- window systems and profiles;
 - window frames;
 - glass sealed units;
 - PVC cellular roofline products such as soffit boards, fascias and cladding;
 - PVC rigid roofline products such as hollow soffits; and
 - PVC window trims.
- 5.2 In its decision, the OFT noted that ‘with regard to the manufacture and supply of window profiles, window frames, and glass sealed units the parties have a minimal overlap’ and it did ‘not consider, on the basis of the available evidence, that concerns arise in these areas’.¹¹ The OFT estimated that the parties’ combined market share was no more than 15 per cent. This estimate is broadly supported by industry reports.¹² We did not identify any issues relating to the parties’ overlap in the manufacture and supply of these products and none of the submissions we received addressed this aspect of the merger. We do not therefore consider the parties’ overlap in these products further. The parties do not overlap in the manufacture of rainwater products.¹³

¹⁰ *Merger Assessment Guidelines, CC2 (revised)*, September 2010 (the Guidelines), [paragraph 3.3.5](#).

¹¹ OFT decision on Epwin, published 9 August 2012, available from www.of.gov.uk/OFTwork/mergers/decisions/2012/epwin.

¹² See, for example, The 2011 Annual PVC-U Window Industry Report in the UK & Republic of Ireland, D&G consulting, Table 22, p54.

¹³ Following the reference from the OFT, the parties clarified that Latium did not manufacture rainwater products.

- 5.3 Our inquiry has concentrated on the parties' horizontal overlap in the manufacture and supply of cellular and rigid PVC-extruded roofline products including fascias, soffits, PVC cladding and twin hollow soffit (roofline) and window trims made by SBP for Epwin and Kestrel for Latium.
- 5.4 The Guidelines state that the purpose of market definition is to provide a framework for the analysis of the competitive effects of the merger.¹⁴ They go on to state that the CC and OFT (Authorities) will identify the market within which the merger may give rise to an SLC. The Authorities' aim when identifying the relevant market is to include the most relevant constraints on the behaviour of the merged companies.
- 5.5 The Guidelines state that:
- Market definition is a useful tool, but not an end in itself and identifying the relevant market involves an element of judgement. The boundaries of the market do not determine the outcome of the Authorities' analysis of the competitive effects of the merger in any mechanistic way. In assessing whether a merger may give rise to an SLC the Authorities may take into account constraints outside the relevant market, segmentation within the relevant market, or other ways in which some constraints are more important than others.¹⁵
- 5.6 The Guidelines also note that in practice the analysis leading to the identification of the market or markets and assessment of competitive effects in the market(s) will overlap, with many of the factors affecting market definition being relevant to the assessment of competitive effects and vice versa.¹⁶ In this section, we set out the relevant market in which we have reached our conclusions on the SLC test, with reference to our assessment of pre-merger competition and the effects on competition of the merger in Sections 7 and 8.

Product market

- 5.7 The parties told us that in their view there was a single product market for PVC and non-PVC roofline products, rainwater products and window-trim products. It said that PVC and non-PVC roofline products should be considered in the same market based on demand-side substitutability, while rainwater and window-trim products should be included based on supply-side substitutability.

Timber roofline products

- 5.8 In considering whether to include products in the same product market on the basis of demand-side factors, the Guidelines state that the CC will consider, among other things, the closeness of competition between different products.¹⁷ The Guidelines further state that the:

Evidence used to assess the closeness of substitution between products may include:

¹⁴ The Guidelines, [paragraph 3.3.5](#).

¹⁵ The Guidelines, [paragraph 5.2.2](#).

¹⁶ The Guidelines, [paragraph 5.1.1](#).

¹⁷ The Guidelines, [paragraph 5.2.15](#).

- information about product characteristics such as physical properties and intended use that can indicate similarities between different products;
- information about relative price levels and the extent to which prices of products within the candidate market are correlated with each other, as compared with the prices of products outside the candidate market;
- information on prices and sales volumes over time or across areas that permit analysis of the way that customers respond to changes in prices or to firms entering and leaving the market;
- responses from customers, competitors and interested and informed third parties to questions—sometimes posed in surveys—about customer behaviour and the hypothetical monopolist test;¹⁸ and
- documents such as marketing studies, consumer surveys prepared in the normal course of business, market analyses prepared for investors, and internal business analyses (eg board papers, business plans and strategy documents).

Views of the parties

- 5.9 The parties told us that there were alternatives to their PVC roofline products and window trims made of other materials, in particular timber. They submitted that timber could be used instead of PVC for roofline and that timber roofline products constrained the pricing of PVC roofline products, with timber being a cheaper though inferior product.
- 5.10 Epwin pointed to a report it commissioned from [REDACTED], which estimated¹⁹ that 41 per cent of fascias, soffits and cladding in the UK were cellular PVC roofline products. [REDACTED] estimated that timber accounted for just over 50 per cent of these roofline products.²⁰ The [REDACTED] report also estimated that there was an approximately 50:50 split in the use of PVC and timber for roofline products in new-build houses.
- 5.11 Epwin also cited responses to the survey we commissioned as part of this inquiry in support of its view that timber roofline products should be considered part of the same product market. Specifically, Epwin highlighted that of those surveyed: 39 per cent of installers used timber as well as PVC for roofline purposes; and 17 per cent of Epwin's stockists also stock timber for roofline use.²¹ Further, 45 per cent of installers cited customer preference as a reason for using materials other than PVC. Epwin said that, in its view, this preference was related to the price at which timber was available.²²

¹⁸ The hypothetical monopolist test is used in market definition. The test is if a hypothetical firm that was the only present and future seller of the products in the candidate market would find it profitable to raise prices (see [paragraphs 5.2.9–5.2.20](#) of the Guidelines).

¹⁹ [REDACTED] had 'not researched volumes for cellular foam profile volumes used in fascia, soffit and cladding applications in the UK compared to timber'. Its estimates were based on 'some limited sampling at times over the last few years' [REDACTED].

²⁰ Roofline products can also be manufactured from aluminium or cement.

²¹ Figure 3.2 of [Survey Report](#).

²² Figure 3.3 of [Survey Report](#).

- 5.12 In support of its submission that customers switched to timber on the basis of price, Latium provided a list of the bids it had submitted for framework agreements to provide builders with materials for new-build housing projects between 2009 and 2012. As a result of the lack of a formal tendering process for these framework agreements, the list was compiled from staff recollections rather than an organized database and Latium did not have definitive information on why bids had not been successful. Nevertheless, Latium submitted that to the best of its knowledge, [redacted] out of [redacted] bids for framework agreements in the specification segment had been lost to suppliers of timber roofline products.
- 5.13 The parties also submitted to us their own analysis assessing the relative installed costs of timber and PVC roofline products. This indicated that the installed cost of timber and PVC roofline products for an installer buying from a stockist would be almost identical. It also showed that the installed cost of using PVC for a house builder negotiating directly with a manufacturer would be approximately £[redacted] cheaper than a timber alternative because of the cheaper prices negotiated by house builders with PVC roofline manufacturers. However, the analysis does not take into account whether a house builder could purchase timber on particularly favourable terms, as is the case with PVC. The parties told us that this was because they did not have access to the contracts between house builders and timber suppliers.

Third party views and other evidence

- 5.14 There is evidence to show that timber may be used instead of PVC for roofline products. PVC roofline products were originally manufactured as a replacement for the timber products traditionally used on UK properties. PVC fascias and soffits are made to resemble timber and have similar properties, for example they can be nailed to a wall or to another part of the roofline. The evidence indicates therefore that the physical characteristics and intended use of timber roofline products are similar to those of PVC roofline products.
- 5.15 Our survey did not support the estimates of timber roofline installation in the [redacted] report submitted by the parties. 57 per cent of installers stated that they did not use timber products at all²³ and of the 39 per cent of installers who also used timber for roofline, 84 per cent stated that they used no more than 25 per cent of timber in their work. Based on the survey results, a reasonable estimated range of the fraction of timber usage in the population surveyed is between 7 and 12 per cent, suggesting that the use of timber is significantly less than the 50 per cent estimate in the [redacted] report.²⁴
- 5.16 Evidence from national house builders also indicates that the estimates in the [redacted] report were too high. House builders told us that PVC roofline products were more durable and generally of higher quality than timber. Nearly all cited planning restrictions as the only reason they would use timber and none suggested that they were regularly using timber where PVC was allowed.
- 5.17 In addition, the evidence indicates that end-users do not switch between timber and PVC roofline products based on changes in price. When asked, none of the 17 national house builders which responded to our questionnaire provided examples of

²³ Figure 3.2 of [Survey Report](#). 3 per cent stated that they did not know—numbers may not add up to 100 per cent due to rounding.

²⁴ Based on Table 34 in the final version of survey results, the calculation is:
 $39\% \times [(0\% \times 3\%) + (25\% \times 81\%) + (50\% \times 9\%) + (75\% \times 1\%) + (100\% \times 5\%)] = 12\%$ for the upper bound and
 $39\% \times [(0\% \times 3\%) + (12.5\% \times 81\%) + (37.5\% \times 9\%) + (62.5\% \times 1\%) + (87.5\% \times 5\%)] = 7\%$ for best estimate.

having switched from PVC to timber in the last five years. Similarly, evidence from stockists and installers suggested that end-users did not switch between PVC and timber based on price. Selco, a large builders' warehouse stocking both PVC and timber roofline products, told us that it had seen growth in PVC products regardless of price. Similarly, builders' merchants such as [redacted] and [redacted], which also stock both types of products, did not report any changes in relative volumes sold of PVC and timber roofline products in response to the changes in their relative prices. Further, our survey indicated that only 4 per cent of installers and 4 per cent of stockists who also used or stocked timber did so because of the initial cost of the product.²⁵

- 5.18 We sought to verify with specification customers the information in Latium's list of bids for framework agreements. [redacted] of the [redacted] bids which Latium considered it had lost to timber were with one major national house builder. The house builder concerned told us that it did not consider non-PVC alternatives as substitutes and that they were 'currently significantly more costly'. Furthermore, it said that it had not switched between PVC and non-PVC products in the past five years.
- 5.19 Third parties from whom we received responses also did not consider that timber acted as a competitive constraint on PVC roofline products. For example, all but one of the six other manufacturers of PVC roofline products told us that they did not consider that timber constrained the price of PVC products; none provided examples of how they had taken into account the cost of timber when setting prices. Of the three stockist chains that stocked both PVC and timber roofline products, none said that prices of roofline products made of one type of material moved in response to changes in the price of those made of the other.

Our assessment of the evidence and conclusion on including timber in the product market

- 5.20 The parties submitted evidence which showed that for house builders the installation price for PVC roofline products was slightly cheaper than for the equivalent timber products. They also told us that they considered that they had lost bids for supplying house builders to timber. The pricing information submitted by the parties was inconclusive because it did not take into account the prices paid by house builders for timber. The evidence from third parties did not support the view that the price of PVC was constrained by the price of equivalent timber products nor that house builders considered timber an alternative. Sales of timber roofline products for new-build properties were driven primarily not by prices but by planning restrictions and in refurbishments price was not a significant factor in installers' decisions about which product to use. We therefore considered that the evidence indicated that although timber roofline products could be used instead of PVC roofline products, they did not, in practice, constrain the price of PVC roofline products in current market conditions.
- 5.21 We therefore conclude that timber roofline products should not be included in our product market definition. Furthermore, as the above evidence indicates that the price of timber does not act as a significant competitive constraint on the price of PVC roofline products, we did not consider timber further in our competitive assessment.

²⁵ Figure 3.3 of the [Survey Report](#).

Rainwater and other PVC-extruded products

The parties' views

- 5.22 Epwin and Latium told us that all PVC roofline, window and rainwater products should be included in the same product market because the products are manufactured using the same basic production process. They said that the costs of switching and expansion were low and all other companies extruding PVC were credible alternatives to the parties and should therefore be included in the same market. They also argued that conditions of competition, in the context of a declining market, were unlikely to be useful guides to supply-side competitive constraints and that other PVC products should be included in the product market on the basis of supply-side factors.

Third parties' views

- 5.23 Manufacturers' views differed on the extent of the similarity between the extrusion processes for different products. [One manufacturer], which currently produces PVC rainwater products and roofline and window-trim products, supported the view of the parties that it was relatively straightforward to switch production between each set of products and within the one-year time frame described in the guidelines. [Another manufacturer] said that there were differences between the manufacturing processes for cellular products, such as roofline and window-trim products, and rigid PVC products such as rainwater products. We further consider the significance of any differences between the two production processes in paragraphs 8.25 to 8.31.
- 5.24 We also received evidence that stockists and end-users generally bought PVC window trims and roofline products from the same manufacturer but sourced rainwater products separately. For example, most stockists told us that they purchased PVC window trims and PVC roofline products from the same manufacturer.²⁶ By contrast, all of the national house builders from which we received responses told us that they bought their rainwater products and roofline products from different companies. Similarly, all except one of the major stockists sourced their rainwater and roofline products separately. The one exception was an integrated stockist which sold its own-brand roofline products.
- 5.25 All the manufacturers which produced PVC fascias and soffits also produced and supplied window trims. While some manufacturers produce both roofline PVC products and rainwater PVC products (eg Epwin, FloPlast and Kalsi), we were told that in many cases roofline PVC products and rainwater PVC products are produced by different manufacturers. Manufacturers which supply PVC rainwater products but not roofline PVC products include Polypipe, Marley, Hunter, Wavin, Hepworth and Brett Martin. Similarly, of the five largest PVC roofline manufacturers pre-merger, according to market share, only Epwin also produced rainwater products.
- 5.26 Additionally, the sale and distribution of rainwater products differ from those of PVC roofline and window-trim products. For example, rainwater products are also usually sold as a system²⁷ because individual components produced by different manufacturers are not compatible, while this is generally not the case for roofline products. Also, while there is some overlap in the distribution networks for roofline and rain-

²⁶ Of the nine large chain stockists which responded to our questionnaire, eight sold fascias, soffits and window trims of which seven sourced all three products from the same manufacturer.

²⁷ Rainwater systems will also include fittings which are injection moulded rather than extruded.

water products, rainwater products are distributed primarily through builders' merchants, while roofline products are distributed mostly through dedicated plastics stockists, further highlighting the differences in conditions of competition between the two products.

Our assessment

- 5.27 The boundaries of the relevant product market are generally determined by reference to demand-side substitution. The Guidelines state, however, that in some circumstances several narrow relevant markets can be aggregated into a single broader one based on considerations about the response of suppliers to changes in prices. The CC may aggregate multiple narrow markets into a single broader one based on supply-side factors considerations, where:²⁸
- (a) production assets can be used by (a) companies to supply a range of different products that are not demand-side substitutes, and the companies have the ability and incentive quickly (generally within a year) to shift capacity between these different products depending on demand for each; and
 - (b) the same companies compete to supply these different products and the conditions of competition between the companies are the same for each product.
- 5.28 The parties argued that the manufacturing process of extrusion is sufficiently similar for many PVC products to allow manufacturers to switch production easily between roofline products and other products, such as rainwater products. This was supported by some manufacturers.
- 5.29 However, we received evidence suggesting different conditions of competition between rainwater products and roofline and window-trim products. Different manufacturers compete to supply the two sets of products, they are often distributed to end-users through different routes, and stockists and end-users source the two sets of products from different manufacturers. We therefore did not consider that roofline and window-trim products should be aggregated in the same product market as rainwater products and other rigid PVC products on the basis of supply-side substitution.

Conclusions on the product market

- 5.30 We therefore conclude that PVC window trims and roofline products are in the same market based on supply-side factors. We do not consider that rainwater goods and other PVC extruded building products should be included in the same product market
- 5.31 We note that there is evidence that manufacturers which produce PVC rainwater products and PVC roofline products have production assets which give them the ability to switch capacity between these two products. We consider the extent of the competitive constraint which this places on the parties in our assessment of swing capacity in paragraphs 8.25 to 8.31. We also consider in paragraphs 8.33 to 8.35 the potential for manufacturers of other PVC extruded goods to enter the market for PVC roofline and window-trim products.

²⁸ Guidelines, [paragraph 5.2.17](#).

Geographic market

- 5.32 Epwin told us that in its opinion the scope of the geographic market should be considered as an area covering northern Europe or, at least, an area comprising the UK, Republic of Ireland, France, Germany, Belgium, Holland and Poland. An industry report by D&G Consulting (D&G) submitted by Epwin generally considers UK and Republic of Ireland manufacturers together based on the volume of trade between the two countries. According to this report, almost all of the 3,400 tonnes of extruded cellular PVC products imported into the Republic of Ireland in 2010 were sourced from the UK. At the same time, it stated that over 90 per cent of the 10,400 tonnes of imports of extruded cellular PVC products to the UK originated in the Republic of Ireland.
- 5.33 End-users purchase PVC roofline and window-trim products through UK stockists and our evidence indicated that, in order to supply these stockists, manufacturers require a distribution base in the UK. For example, the parties told us that stockists held little stock at any one time, often requiring [✂] deliveries per week, and we found that the evidence indicates that stockists are not being supplied with significant volumes directly from overseas.
- 5.34 Some non-UK manufacturers have set up distribution bases in the UK to supply stockists. For example, FloPlast is a UK manufacturing and distribution company which sources its PVC roofline products from a related company in the Republic of Ireland, Cork Plastics. Similarly, Plastivan UK distributes PVC roofline products to UK stockists from its base in Bristol. It told us that it sourced most of its products from its parent company which manufactured in Belgium.
- 5.35 The evidence showed that the distribution and supply of PVC roofline and window-trim products occurs from within the UK. We noted that distribution outlets may source products manufactured outside the UK, and particularly from the Republic of Ireland, and we considered the potential for other European manufacturers to establish a UK distribution base in our assessment of entry and expansion in Section 8.
- 5.36 Each of the eight manufacturers currently supplying UK stockists, which responded to us, said that it supplied at least across the UK and that wholesale prices did not vary by region. House builders told us that they did not require a local or regional presence from the manufacturer as the goods were distributed through stockists. This evidence indicated that the geographic market for the manufacture and supply of PVC roofline and window-trim products for retail in the UK is not narrower than the UK.
- 5.37 We therefore define the geographical market as the UK.

Conclusions on market definition

- 5.38 Our conclusion is that the relevant market for the purposes of our statutory questions in this inquiry is the supply of PVC roofline products and window-trim products within the UK.

6. Counterfactual

- 6.1 We must decide if the merger has resulted, or may be expected to result, in an SLC. To do this, we considered what would have happened had Epwin not acquired Latium, Building Plastics and CET. This situation, referred to as the counterfactual, is the benchmark against which we compared the competitive effects of the merger.²⁹
- 6.2 In connection with consideration of the counterfactual, the parties made a number of points about Latium's financial and operational performance pre-merger. These included [REDACTED].
- 6.3 The Guidelines state that:
- In forming a view on an exiting firm scenario, the Authorities will consider:
- (a) whether the firm would have exited (through failure or otherwise); and, if so
- (b) whether there would have been an alternative purchaser for the firm or its assets to the acquirer under consideration; and
- (c) what would have happened to the sales of the firm in the event of its exit.³⁰
- 6.4 We considered the financial and operational issues affecting the Latium businesses pre-merger. We considered whether in light of the financial and operational factors highlighted by the parties, Latium would have exited the market. Our assessment primarily concerned Latium's subsidiary Kestrel, as this is the company which manufactures the products giving rise to potential competition concerns (see paragraph 5.3). Other companies acquired by Epwin as part of the merger, or owned separately by Mr Kennedy, are relevant to the counterfactual to the extent that Kestrel's relationship with those companies might have affected its future prospects.

The pre-merger situation

- 6.5 The parties told us that the [REDACTED]. They said that this was reflected in Kestrel's profitability. Its operating profit margin was already low in 2007, at about [REDACTED] per cent, and had [REDACTED] between 2007 and 2011.
- 6.6 The parties also said that [REDACTED]. Kestrel outsourced its warehousing and logistics operations to Trentham, which operates a warehouse at Trentham Lakes. This resource is shared between Kestrel and Spectus. The rent and terms of the lease [REDACTED]. The head lease on the warehouse [REDACTED] and the annual cost of the lease and business rates on the property is around £[REDACTED]. Latium told us that the warehouse [REDACTED] had [REDACTED] per cent utilization. [REDACTED]³¹
- 6.7 Latium told us that [REDACTED].
- 6.8 Bank of Scotland provided banking facilities to Latium [REDACTED].

²⁹ The Guidelines, paragraph 4.3.1, state: 'The application of the SLC test involves a comparison of the prospects for competition with the merger against the competitive situation without the merger. The latter is called the "counterfactual".'

³⁰ The Guidelines, paragraph 4.3.8.

³¹ Latium told us [REDACTED].

The views of the parties

- 6.9 In Epwin's opinion, [REDACTED]. Latium agreed that the most likely consequence of the Epwin merger not having been concluded was that at some time in the next 6 to 24 months, [REDACTED].
- 6.10 Latium told us that [REDACTED].
- 6.11 The parties further submitted that, in their opinion, [REDACTED].
- 6.12 Latium told us that if Kestrel had remained under its ownership, it would have expected the business to continue to decline and lose market share. [REDACTED]
- 6.13 Latium told us that it did not approach any other parties about a sale of Kestrel in the period immediately prior to the merger. It also said that no discussions with potential purchasers of Latium, Building Plastics and CET took place other than with Epwin.

Views of Bank of Scotland

- 6.14 Bank of Scotland told us that it had been concerned about its loans to Latium [REDACTED]. It said that it was looking to remove its exposure to these loans through, in order of preference, the participation of another bank, an injection of equity finance, or a voluntary or enforced sale of the business.
- 6.15 The bank told us that a further deterioration in Kestrel's trading performance would most likely [REDACTED]. The bank said that Latium had complied with its covenants from January 2011 up until the merger in January 2012. It also told us [REDACTED].
- 6.16 The Epwin deal enabled [REDACTED] Bank of Scotland's [REDACTED].

Potential alternative purchasers

- 6.17 We asked a number of the parties' competitors, and stockist chains, whether they would have been interested in acquiring Kestrel if they had known it was for sale. Eurocell said that it would have been interested at around the time Epwin and Latium were negotiating in mid-2011. Eurocell also told us that current market conditions were now less favourable than in 2011 and as a result they were no longer sufficiently favourable to make such an acquisition attractive. Freefoam indicated that it would have been interested in acquiring Kestrel. Gap/Homeline told us that it would have been interested but did not have available funding. Two major stockists, [REDACTED] and [REDACTED], told us that they would not have been interested.

Our assessment of the counterfactual

- 6.18 Appendix C sets out our financial analysis of Latium and Kestrel. It shows that the underlying business of Latium had a positive EBITDA³² in the 14 months ended 31 December 2011 of £[REDACTED].³³
- 6.19 [REDACTED]

³² Often used as a proxy for cash trading profit.

³³ The profitability of Latium and Kestrel are used interchangeably in our analysis, because for all practical purposes Kestrel was the only trading company owned by Latium.

- 6.20 Our financial analysis of Latium and Kestrel in Appendix C showed a deteriorating trading performance between the year ended 31 October 2010 and 14 months ended 31 December 2011. One stockist, [REDACTED], told us that [REDACTED].
- 6.21 However, as we have noted, Latium was a profitable business and had not breached its banking covenants in the 12 months preceding the merger. Furthermore, [REDACTED].
- 6.22 We note that Bank of Scotland was looking to remove itself from its banking arrangements with Mr Kennedy's companies. As we note in paragraph 6.20, there is evidence that there would have been potential interest in the Kestrel business from at least two other parties in mid-2011. If [REDACTED], it is likely that the number of prospective buyers would have increased as the business would have been available at a lower price and would have been potentially more attractive [REDACTED].
- 6.23 We note that other producers of roofline products have been put into administration and subsequently acquired without having been broken up. For example, GAP bought the assets of Everwhite in 2009.
- 6.24 We note that Latium, Building Plastics and CET were valued at nearly 50 per cent of the combined entity at the time of the merger.³⁴ This suggests that Epwin saw value in the combined companies and others may have too. The synergy benefits cited by Epwin as the rationale for the merger, [REDACTED], and the evidence we received from third parties, suggest that the most likely alternative purchaser would have come from another company or group extruding PVC building products.

Conclusions on the counterfactual

- 6.25 Our conclusion is that, in the absence of the merger with Epwin, Latium would most likely have been sold to a third party either by a process of negotiation or through administration. The purchaser would, in our view, most likely have been a company involved in the extrusion of PVC building products either inside or outside the market for PVC roofline and window trim products. For the purposes of assessing the competitive effects of the merger, we consider the appropriate benchmark to be competition between an independent Latium and Epwin. The counterfactual is therefore the continuation of the conditions of competition prevailing before the merger. We assess the potential implications of the merger against this benchmark in Section 8.

7. The nature and extent of pre-merger competition

- 7.1 In this section we estimate all parties' shares of supply of PVC roofline and window trims and describe two customer segments we have identified. We then set out the framework for our assessment of competition based on the bilateral negotiations through which transactions are carried out. We consider three features: the extent of product differentiation; the extent to which any switching costs we have identified might provide a barrier to customers changing supplier; and the estimated level of spare capacity in the market.

³⁴ 50 per cent is a rounding of the 53 / 44 per cent share split of the merged entity between Mr Rawson, Mr Kennedy and other shareholders at the time of the merger.

The UK market for the supply of PVC roofline and window-trim products

Suppliers

7.2 Prior to the merger, Epwin and Latium were the two largest suppliers of roofline and window-trim products in the UK by turnover. They competed with a number of other companies which produce and/or distribute these products within the UK, the largest three of which we describe below. Table 1 shows the CC's estimates of shares of total turnover in 2011 in the UK roofline and window-trim market.³⁵

TABLE 1 Turnover and estimated market shares of suppliers to the UK PVC roofline and window-trim market

Company	Total 2011 roofline and window-trim turnover (CC market definition) £	Estimated 2011 market share %
Epwin	[£]	[20–30]
Latium	[£]	[10–20]
Post-merger	[£]	[30–50]
Eurocell	[£]	[10–20]
Freefoam	[£]	[10–20]
GAP/Homeline	[£]	[5–10]
FloPlast*	[£]	[5–10]
Kalsi	[£]	[0–5]
LB Plastics	[£]	[0–5]
Eagley Plastics	[£]	[0–5]

Source: Submissions and CC analysis.

*FloPlast is a UK manufacturer and distributor for a related company, Cork Plastics, which manufactures in the Republic of Ireland.

Note: Percentages may not add up to 100 due to rounding.

7.3 Based in Alfreton, Derbyshire, Eurocell is a manufacturer and distributor of PVC building products including roofline, window trims, conservatory roofs, doors, sealants and fixings with its own chain of 126 stockists. Eurocell also owns the Deeplas brand of roofline products, which it sells to independent stockists across the UK and exports to Belgium for distribution to independent stockists in France and the Benelux countries.

7.4 Freefoam manufactures PVC roofline, cladding, window-trim and rainwater products in Northampton for supply to UK customers. Freefoam also manufactures these products in Cork, Republic of Ireland, for supply to the Irish and Continental European markets. Freefoam does not own any stockists and sells to independent stockists.

7.5 Homeline Building Products (Homeline) is a manufacturing business with sites in Aberdare, South Wales, and Blackburn, Lancashire. It is the brand of the stockist GAP. Homeline manufactures PVC building products including fascias, soffits, window trims and sills.

³⁵ We note that a small number of manufacturers did not respond to our questionnaire, so the estimated market shares should technically be considered as upper bounds. However, given the small supply by those that did not respond, their exclusion does not make a material difference to estimated market share figures.

Trade segment

- 7.6 As noted in paragraph 2.12, we have identified two broad customer segments for whom the route to market differs slightly. The majority of customers buy PVC roofline and window-trim products over the trade counter from stockists. We term this the trade segment. In this segment, stockists buy the product from a manufacturer and sell it on to the customer. The parties told us that at both stages of the supply chain there was a price negotiation, often against a benchmark provided by the manufacturer's price list. Thus the manufacturer's profit margin depended on its negotiation with the stockist and the stockist's profit margin also depended on its negotiation with the customer.

Specification segment

- 7.7 The other customer segment, which we refer to as the specification segment, is generally represented by national or regional house builders and large contractors. These customers often specify their product requirements and negotiate prices directly with manufacturers. Since these are large customers, they are generally in a position to negotiate a better price than would be achieved by a customer negotiating over the trade counter. The products are nonetheless supplied to the customer through stockists. The manufacturer agrees with the nominated stockist an appropriate margin for these sales, taking account of any ancillary services provided by the stockist, such as delivery to the site. This generally involves a payment, known as 'contract support', being made by the manufacturer to the stockist.³⁶ Thus a stockist's access to these sales and its margin are determined entirely by agreement with the manufacturer, rather than as a result of any negotiation with the end-customer.
- 7.8 The parties estimated, and third parties agreed, that the new-build sector represented around 10 to 15 per cent of roofline and window-trim sales. The parties also told us that other specification sales, for example to contractors refurbishing social housing stock, represent approximately a further [3-5] per cent of their business, suggesting that the specification sector represents no more than [20-30] per cent of the total market. The parties told us that any end-user could try to negotiate directly with a manufacturer and thus become part of the specification segment, though it appears that in practice it is only purchasers of large volumes which do so.
- 7.9 Manufacturers and stockists told us that the parties had a particularly strong presence in the specification sector. We gathered information from stockists and end-users on the manufacturers which supplied PVC roofline and window-trim products to the largest 15 national house builders (as ranked by turnover according to the Construction Index³⁷). Table 2 shows the suppliers of PVC roofline and window-trim products to these 15 UK house builders.

³⁶ The parties describe these arrangements as framework agreements and we were told that there were no formal contracts between the manufacturer and the house builder.

³⁷ The Construction Index provides information services for the construction industry. Its ranking of the top 20 house builders by turnover is available from www.theconstructionindex.co.uk/market-data/top-20-house-builders/2011. National house builders are the largest purchasers in the specification segment.

TABLE 2 Suppliers to the top 15 national house builders

Rank in 2011	House builder customers	Supplier of PVC roofline and window trim
1	Taylor Wimpey	Kestrel exclusive (Latium)
2	Barratts	Swish exclusive (Epwin)
3	Persimmon Homes Plc	Swish exclusive
4	Bellway	Swish, Kestrel and Freefoam
5	Berkeley Homes	Kestrel, Swish
6	Redrow	Celuform exclusive (Latium)
7	J S Bloor	Eurocell exclusive
8	Bovis	Swish exclusive
9	Crest Nicholson Plc	Freefoam exclusive
10	Miller Homes	Eurocell
11	GallifordTry	Freefoam exclusive
12	Stewart Milne Group	Swish
13	Countryside Developments	Swish
14	McCarthy Stone	No manufacturer agreements in place
15	CALA	No manufacturer agreements in place

Source: Stockist and house builders' submissions.

7.10 This list of suppliers supports the views of stockists and competitors that the parties are particularly strong in the supply to specification customers. Before the merger, there were four manufacturers supplying to the top 15 house builders (Epwin, Latium, Freefoam and Eurocell). FloPlast and Homeline/Gap do not currently supply to any of the top 15 house builders but two of them listed FloPlast and one Homeline/Gap as potential suppliers. Homeline/Gap told us that it did supply to a relatively small part of the specification segment.³⁸ National house builders told us that they required national distribution coverage and a full range of all roofline and window-trim products.

The bargaining framework

7.11 The parties told us that, regardless of the different routes to market, interactions for the purchase of PVC roofline and window-trim products are characterized by frequent bilateral negotiations. This view of the market was supported by third parties. [A stockist] told us that prices were negotiated as part of its annual trading agreement and further price deals were negotiated locally by branches. Similarly, 81 per cent of stockists³⁹ and 69 per cent of installers surveyed negotiated prices at least once a year with 28 per cent of installers negotiating every time they purchased the product.⁴⁰

7.12 We characterize this way of purchasing products as a bargaining framework. In such a bargaining framework, the relevant issue for buyers is their alternative or 'outside option'. In economic terms, the outside option is the next best alternative or business proposition of buyers in case their negotiations with a given supplier break down. Intuitively, buyers with a good outside option can negotiate a good deal because they have a credible and favourable alternative to choose from if the negotiations break down. As such, they can 'leave the negotiating table'. In contrast, buyers with no outside option, or a poor one, will have to accept a worse deal because their bargaining position is weak.

7.13 In a bargaining framework, the main factors affecting the outside option of the buyers are:

³⁸ Gap/Homeline told us that it had a turnover of approximately £1 million to the specification segment.

³⁹ Figure 5.7 of [Survey Report](#).

⁴⁰ Figure 5.11 of [Survey Report](#).

- (a) The degree of product homogeneity or differentiation. If products are very different, buyers' preferences for a specific product will be higher. In such cases, switching to another product entails loss of utility and worsens a buyer's outside option. In contrast, with perfectly homogeneous products, all else being equal, all alternative suppliers are equally desirable.
- (b) Switching costs. For a customer locked into a commercial relationship with substantial switching costs, the outside option is less desirable. Therefore, switching costs create incumbency advantage.
- (c) Capacity constraints of alternative suppliers. Suppliers may not be credible alternatives if they are capacity constrained.

7.14 We consider below each of these factors in the context of the UK PVC roofline and window-trim market.

The extent of product differentiation

7.15 There are a number of potential sources of product differentiation for roofline and window-trim products. These include factors intrinsic to the products, such as their quality, size and colour. Differentiation may also occur on the basis of service quality, technical support and branding which are specific to the company that manufactures the product rather than the product itself. We considered the evidence on product-specific and firm-specific differentiation below, taking into account the extent to which customers consider these factors when making purchasing decisions.

Product-specific differentiation

- 7.16 The parties told us that, in their view, the products concerned were homogeneous and of a standard specification. As such, they could readily be produced by a number of different manufacturers. Competitors' product ranges and shapes were very similar rather than identical but the parties told us that products were generally indistinguishable between manufacturers which used similar tools and processes.
- 7.17 The parties' competitors broadly confirmed this view of the products. Three of the four largest competitors to the parties addressed the issue of product differentiation. Eurocell told us that its range was slightly differentiated compared with its competitors on fascia appearance, density and shades of white. While it was possible to tell the difference between its products and other manufacturers, Eurocell said that for the builder in the trade segment purchasing decisions were about service and convenience rather than the finish of the product. Freefoam noted that there were no specific product differences in terms of what end-users wanted. FloPlast told us that products were largely homogeneous and competition was predominantly on price.
- 7.18 We received responses from two manufacturers of other PVC-extruded products. Both Veka and Deceunick drew a distinction between the window profiles they extruded and roofline products. They both described roofline as 'commodity' products. Two of the national house builders used the same or similar descriptions. Galliford Try told us that it generally considered roofline products to be 'generic'. Similarly, Bovis described roofline as a 'commodity'.
- 7.19 Three other national house builders did make general references in their written submissions to quality or product performance as factors affecting their purchasing decisions. Similarly, quality was highlighted as an important factor in our survey of installers and stockists. For example, when asked what was important when choos-

ing products, the quality of the product itself was the overriding consideration—quality (76 per cent very important), durability (67 per cent very important) and appearance (66 per cent very important).⁴¹ This emphasis on quality might be indicative of some degree of product differentiation.

- 7.20 However, we noted that two of the three builders that raised quality as an issue in their written submissions, used PVC roofline and window-trim products from more than one manufacturer. This suggested that, for these builders at least, more than one manufacturer meets their quality requirements.
- 7.21 We also heard that quality had been inconsistent in the past but was now becoming much less of a concern. For example, Bovis told us that its main quality considerations were appearance and colour guarantees. There had been problems affecting the colour of PVC roofline in the mid-1990s but Bovis had not experienced such issues for many years. This is consistent with information from the merging parties that problems with roofline products' colour that had occurred in the past had been overcome. Similarly, D&G's industry report notes that 'products have significantly improved in performance, range, quality and appearance over the past few years'.⁴²
- 7.22 We also noted that in our survey, regardless of which manufacturer they bought from, stockists gave the same reasons for choosing a manufacturer: quality of the products; price; quality of service; relationship with the manufacturer; range and availability.⁴³ This is consistent with products being relatively homogeneous in the sense that customers with broadly similar preferences use products from different manufacturers.
- 7.23 Our survey did suggest that there may be product differentiation to the extent that products from different manufacturers are not compatible on the same building, though on this point the evidence was mixed.⁴⁴ We note that even where products of different manufacturers are not interchangeable on a given installation, this is not necessarily indicative of significant product differentiation. For example, two different manufacturers' products would generally be alternatives at the point when decisions are made about which to use on a particular installation.

Company-specific differentiation and branding

- 7.24 Epwin told us that it attempted to differentiate itself from its competitors on the basis of quality of service, particularly the frequency and reliability of its deliveries, and technical support, for example its estimating service.
- 7.25 Large stockist chains cited service and support as factors in their purchasing decisions, but these were generally secondary to price and product quality. For example, Jewson told us that supply decisions were based on 'quality, price and back up support'. Similarly, SIG said that any differentiation that there was between manufacturers was 'derived from price, back sales support, marketing support and

⁴¹ Figure 5.2 of [Survey Report](#).

⁴² *The PVC roofline industry: UK and Ireland Market and Forecasts to 2013*, Spring 2012 edition, D&G Consulting, p8.

⁴³ Figure 5.4 of [Survey Report](#). There are some differences in proportions, with a larger proportion of those using suppliers other than Epwin or Latium doing so because of price, and a smaller proportion doing so because of the quality of the product.

⁴⁴ Of 192 installers sampled, 49 per cent stated that different brands of roofline and window-trim products could not be used interchangeably on a given installation; 47 per cent of installers sampled said that brands could be used interchangeably at least in some cases (Figure 4.2 of [Survey Report](#)).

service proposition'. In our survey, stockists cited service, quality of product and price as the most important factors when choosing a manufacturer.⁴⁵

- 7.26 Epwin also told us that it used its different product brands for different customers. Epwin used its Swish brand almost exclusively to supply the specification segment. Epwin said that this [✂]. Other brands, such as Summit and Concord,⁴⁶ enabled Epwin to meet customers' wishes to differentiate themselves from other stockists, including Epwin stockists, in local areas. Epwin told us that its portfolio of brands, other than Swish, had arisen largely for historical reasons and through acquisitions. One other manufacturer had more than one brand. The main brands in the market and the manufacturer for each are shown in Table 3.

TABLE 3 PVC roofline brands by manufacturer

	<i>Epwin</i>	<i>Latium</i>	<i>Eurocell</i>	<i>Homeline/ GAP</i>	<i>Kalsi</i>	<i>Anglian</i>	<i>LB Plastics</i>	<i>MFP</i>
1	Swish	Kestrel	Euroboard	Homeline	Aquacel	Anglian	Hometrim	Eavemaster
2	Summit	Celuform	Deeplas					
3	Concord	BCE						
4	Quay							
5	Plaslyne							

Source: Main and third parties.

- 7.27 The different brands were seen by some in the market as at different levels of specification. For example, the house builder, Redrow, described Swish (Epwin) and Celuform (Latium) as the two premium brands, with other products from Epwin, Latium and other manufacturers 'perhaps not at the same level of specification'. Also, 39 per cent of survey respondents (stockists and installers) thought brand was important or very important when choosing a roofline product.

- 7.28 The majority view, though, was that brand was not an important factor. Of the 17 national house builders from which we received responses, none other than Redrow mentioned brand as a factor when invited to list the factors that were important when choosing a supplier. Furthermore, when asked to list the three most important factors when choosing roofline and window-trim products, only 3 per cent of respondents to our survey mentioned brand.⁴⁷

- 7.29 The parties told us that [✂].

Pricing

- 7.30 One indicator of potential product differentiation would be the relative prices of different manufacturers' products and different brands sold by the same manufacturer. As we note in paragraph 7.11, prices for PVC roofline products and window trim products are set following a process of bilateral negotiations between the manufacturer and stockist, and often again between the stockist and the end-user. As a result, there are no reliable sources of pricing data at the level of detail of individual products. List prices provide the starting point for negotiations but the parties, corroborated by others, told us that the list prices could sometimes be discounted by as much as 70 to 80 per cent depending on the negotiations. We were able to infer prices at a

⁴⁵ Figure 5.4, [Survey Report](#).

⁴⁶ Epwin sells a Windowstore brand used in its Windowstore outlets and a Plaslyne brand. It also sells stockist-branded goods if stockists request it and sells a Quay brand through its own chain of Quay stockists.

⁴⁷ Figure 5.3 of [Survey Report](#).

higher level from volume sales to, and total prices paid by, stockists. We have therefore sought to provide a robustness check of our qualitative evidence by analysing this data.

- 7.31 In doing so, we attempted to test empirically what a comparison of prices would tell us about the relative homogeneity of products of different manufacturers and different brands. More specifically we assessed:
- (a) the scale of price differences between PVC roofline and window-trim products of different manufacturers (reflecting company-specific, as opposed to product-specific, differentiation); and
 - (b) the scale of price differences between PVC roofline and window-trim products of different brands from the same manufacturer (a potential indicator of product differentiation between brands).
- 7.32 Our analysis of customer-level and brand-level data on Epwin's and Kestrel's sales was relatively inconclusive on the extent to which products are homogeneous. In general, there is a modest difference between the sales value per kg of Epwin and Kestrel products, [REDACTED]. However, such variations may be attributable to differences in product mix and consumer profiles rather than product differentiation. Moreover, as much trade in this market occurs through bilateral negotiations, some degree of price heterogeneity is to be expected.
- 7.33 An examination of brand-level data shows [REDACTED].
- 7.34 The details of our analysis of pricing data can be found in Appendix D.
- 7.35 We noted, in particular, the broad consensus of views from the parties' competitors and customers that the products concerned are commodity products which are broadly homogeneous.
- 7.36 In our view, the evidence from end-users suggested that they required suppliers to meet a minimum quality standard. The minimum quality standard is not incompatible with viewing the product as relatively homogeneous. Some end-users and stockists differentiate on the basis of brand but they were in the minority. Our pricing analysis indicates that branding does not enable manufacturers to sell different brands at significantly different prices.
- 7.37 Our view was therefore that the evidence we have received was consistent with a relatively homogeneous product being sold.

Switching costs

- 7.38 Based on our view that products are relatively homogeneous, we would expect customers to have incentives to switch manufacturers in response to changes in price. We therefore sought to establish how easy it is for stockists and end-users to switch manufacturer and any costs involved in switching.
- 7.39 There are two points in the supply chain for PVC roofline and window-trim products where potential switching costs are relevant: an end-user's ability to change manufacturer; and a stockist's ability to change supplier and thus supply the end-user with a different product. We therefore assessed the evidence on switching costs for stockists and end-users.

Stockists

The parties' view

- 7.40 The parties told us that stockists could switch between manufacturers within a single month. Epwin said that when it acquired a chain of independent stockists, it had switched sourcing of the products from another manufacturer to one of its own brands with no significant additional business costs or stock write-offs.

Third parties' views

- 7.41 Other manufacturers broadly supported this view. Seven of the nine manufacturers from which we received responses said that it was relatively easy for stockists to change supplier.
- 7.42 Of the nine large regional or national stockists we spoke to, only two considered it difficult to change manufacturer. The two which said it was difficult pointed to the costs arising from a need to write off redundant stock from the original manufacturer.⁴⁸ This was because products of different manufacturers were slightly different in appearance, and that customers often required a full range, for example if re-furbishing the whole roofline on a property.
- 7.43 The results from our survey of stockists were more mixed. Of the 148 Epwin and Latium stockists sampled, 50 per cent regarded changing suppliers as either very easy (22 per cent) or quite easy (28 per cent); 44 per cent of stockists considered it either quite difficult (30 per cent) or very difficult (14 per cent).⁴⁹
- 7.44 However, the results of the survey also indicated that stockists would switch in response to increases in price. When asked how they would respond to a 5 per cent price increase by the parties relative to other suppliers, 67 per cent of stockists said that they would change supplier or reduce the amount they sourced from the parties. This rose to 81 per cent for a 10 per cent price increase.⁵⁰
- 7.45 The proportion of stockists which have or who have not changed manufacturers in recent years is broadly split. From the survey, 19 per cent of stockists had never changed their roofline supplier, while 36 per cent had done so four or more years ago. However, 15 per cent of stockists had changed roofline suppliers within the last year, while a further 25 per cent had done so in the last one to three years.⁵¹

Our assessment of switching costs for stockists

- 7.46 Most of the manufacturers and large stockists said that it was relatively easy for a stockist to change supplier. The evidence we received suggested that the only cost involved resulted from a stockist being left with redundant stock when changing supplier.
- 7.47 Of the smaller stockists we surveyed, 40 per cent had switched manufacturer in the last three years. The results of the survey also showed that stockists would switch in

⁴⁸ The costs of redundant stock would be less of an issue for the stockists which already multi-source. Multi-sourcing is discussed in more detail in paragraph 8.47.

⁴⁹ Figure 5.6 of the [Survey Report](#). The remaining 7 per cent either did not know or refused to answer.

⁵⁰ Figure 6.6 of the [Survey Report](#).

⁵¹ Figure 5.5 of [Survey Report](#).

response to price increases suggesting that any switching costs involved would not prevent stockists from switching.

- 7.48 Our view therefore was that switching costs were not a significant barrier preventing stockists from changing supplier.

End-users

- 7.49 In assessing the potential switching costs for end-users, we have considered the evidence for the two customer segments we have identified: large end-users in the specification segment and installers in the trade segment.

The parties' views

- 7.50 The parties said that in their view there were no meaningful barriers to end-users switching between manufacturers of PVC products because the products concerned were homogeneous and of a standard specification. As such, the parties said that they could readily be produced by a number of different manufacturers.

Third parties' views

- 7.51 Of the 17 house builders that responded to the questionnaire, all but one stated that switching suppliers was not difficult. One identified some potential costs from updating its order schedules for each site.⁵² We found little evidence of actual switching by house builders. None of the 17 that responded to us said that they had changed supplier in the last five years, though five provided evidence that they were multi-sourcing roofline products and window trims. House builders also considered that they had buyer power as large purchasers and that they could negotiate competitive prices with their existing supplier after regularly testing prices in the market.
- 7.52 The evidence from the survey is that installers do not have particular loyalty to manufacturers or brands and find it easy to change stockist. Of 192 installers sampled, 83 per cent regarded changing stockists as easy, based on past experience, including 48 per cent that regarded it as very easy. Only 9 per cent of installers regarded changing stockists as difficult, on the basis of past experience.⁵³

Our assessment of the switching costs of end-users

- 7.53 The overwhelming weight of evidence from end-users indicated that switching manufacturer is relatively easy. The low instances of actual switching by large house builders are not necessarily indicative of high switching costs. House builders were generally of the view that they could negotiate prices with their current manufacturer after testing the market. The evidence indicates there are no material switching costs for end-users.

Our overall assessment of switching costs

- 7.54 Our view is that switching costs are not a sufficiently high barrier to prevent stockists from changing supplier and that there are no material switching costs for end-users.

⁵² The parties told us that one of the services they offered house builders currently using different suppliers was to update their schedules to remove this potential disincentive to change.

⁵³ Figure 5.12 of the [Survey Report](#).

Spare capacity

- 7.55 The third factor we have considered which may affect the outside option of buyers is the level of spare capacity in the market.⁵⁴
- 7.56 Measuring accurately spare capacity in the manufacture of PVC roofline and window trims is very difficult. This is because estimating how much more a manufacturer could produce in response to an increase in demand involves a series of assumptions about labour and machinery. We have adopted a cautious approach and in our assessment of the effects of the merger in Section 8 we adopt what we consider to be a conservative estimate of spare capacity. Appendix E describes the methodology and the result of our calculation of estimates in more detail. These are summarized below.

View of the parties

- 7.57 Epwin told us that there was significant overcapacity in the industry. It said that the overcapacity had been created by declining demand since the industry peak in 2006. Epwin also said that no significant assets had left the industry since that time and there were examples of subsequent new entrants to the market and expansion of capacity by existing manufacturers. Epwin further argued that the decrease in total industry supply from approximately 111,000 tonnes in 2003/04 to approximately 70,000 tonnes in 2010 was indicative of significant spare capacity.
- 7.58 Epwin submitted detailed economic analysis of the relevance of spare capacity and the ability of competitors to increase supply. Epwin's first submitted analysis of the level of spare capacity in the roofline and window-trim market relied heavily on D&G's estimate of industry capacity utilization. D&G estimated that the level of capacity utilization in the market is currently 40 per cent, implying spare capacity of 60 per cent. Epwin subsequently submitted further capacity analysis which suggested that industry spare capacity is 43 per cent.

Third party views

- 7.59 The estimates we received from other manufacturers of their own spare capacity supported the view of the parties that there was significant spare capacity within the market. We consider these estimates in more detail below and in Appendix E. Some manufacturers also told us that they thought there was spare capacity in the market. For example, two of the smaller manufacturers, and one which had exited the market because it viewed it as 'non-profitable', referred to overcapacity in the market.

Our assessment of spare capacity

- 7.60 Information received from third parties and our analysis of the D&G methodology suggested that the D&G estimate of 60 per cent spare capacity was overstated. We asked manufacturers to estimate their spare capacity and most estimated it to be between 20 and 30 per cent. Also, we found that D&G overestimated the maximum output per extruder which it applied to the number of extruders across the industry to reach its capacity estimates. The estimate did not take into account factors such as

⁵⁴ We consider separately in our assessment of the effects of the merger the potential for the parties to be constrained by swing capacity. This is where manufacturers which produce both roofline products and other PVC-extruded products can switch capacity in the production of one set of products to the other.

the age of the machinery, the type of product being extruded and the efficiency of other parts of the production process.

- 7.61 Epwin’s statement that there had been no significant reduction in the productive assets in the market was not supported by [REDACTED], which reported a 19 per cent decrease in the number of cellular foam profile extruders from 161 in 2004 to 130 in 2010. We also noted that, in the case of some producers, such as [REDACTED], due to inadequate maintenance, the operating efficiency of machinery may have deteriorated since 2003/04. This would reduce their productive capacity, even with the number of extruders being constant. Thus, comparing current production levels with their 2003/04 peak was likely to give a misleading estimate of market spare capacity.
- 7.62 We therefore sought to develop a reasonable estimate of the amount of spare capacity in the industry as a whole, and for individual market participants, as well as an estimate of the industry-wide rate of capacity utilization. Our preferred methodology for doing this was to apply manufacturers’ own estimates of their spare capacity to their production in 2011⁵⁵ and aggregate the results for an estimate of industry spare capacity. This involved using a weighted average of spare capacity for each manufacturer taking into account the different estimates of spare capacity for different products provided by some manufacturers.
- 7.63 This methodology is preferable to others because it is the only one that enabled us to estimate the spare capacity of individual manufacturers. Estimates of individual spare capacity are important to our analysis as the outside options of customers may differ, for example depending on whether or not they can buy from manufacturers which are vertically integrated.
- 7.64 The results of this analysis are shown in Table 4.

TABLE 4 **Manufacturer-level spare capacity estimates 2011 for roofline and window trim products**

<i>Company</i>	<i>Total output tonnes</i>	<i>Utilization rate %</i>	<i>Capacity tonnes</i>	<i>Spare capacity tonnes</i>
Epwin	[REDACTED]	[REDACTED]	[REDACTED]	5,000
Latium	[REDACTED]	[REDACTED]	[REDACTED]	6,900
Eurocell	[REDACTED]*	[REDACTED]	[REDACTED]	2,800
Freefoam	[REDACTED]†	[REDACTED]	[REDACTED]	3,400
Homeline Plastics	[REDACTED]	[REDACTED]	[REDACTED]	1,500
Cork Plastics (FloPlast)	[REDACTED]‡	[REDACTED]	[REDACTED]	2,200
Eagley Plastics	[REDACTED]	[REDACTED]	[REDACTED]	1,300
Kalsi	[REDACTED]†	[REDACTED]	[REDACTED]	700
Anglia	[REDACTED]	[REDACTED]§	[REDACTED]	0
LB Plastics	[REDACTED]	[REDACTED]	[REDACTED]	800
MFP	[REDACTED]†	[REDACTED]	[REDACTED]	200
Total	[REDACTED]		[REDACTED]	24,700

Source: Responses to market questionnaires, CC analysis; D&G 2011 report.

*Eurocell provided volumes going through its vertically-integrated stockists only.

†Indicates that the producer did not respond to our question on output, so output levels are taken from D&G’s 2011 report.

‡Cork Plastics’ total roofline output is inferred from statements about the total amount of its production accounted for by roofline products.

§Indicates a conservative assumption that the producer is at full capacity.

Note: Figures rounded to nearest hundred.

- 7.65 These estimates suggest total spare capacity in the region of 25,000 tonnes, amounting to approximately 25 per cent of total capacity. This comprises approximately 12,000 tonnes of spare capacity attributable to the merging parties, and around

⁵⁵ Where parties did not provide production figures for 2011 we used the 2010 estimates in the D&G 2011 report.

13,000 tonnes of spare capacity attributable to the parties' competitors. According to this analysis, five of the parties' competitors have spare capacity in excess of 1,000 tonnes, with two having spare capacity greater than 2,500 tonnes.

- 7.66 Where data was missing in developing these estimates, we adopted a conservative approach in the absence of any robust alternative. For example, where we had no estimate of spare capacity from individual manufacturers or for particular types of product, we included the relevant output but assumed no spare capacity. It was not possible to include the Belgian manufacturer, Plastivan, which supplies to the UK market through its subsidiary Plastivan UK because we did not have data on its output or spare capacity.
- 7.67 We checked our estimate for robustness using two alternative methods to estimate industry-wide capacity utilization and spare capacity.⁵⁶ First, as explained in Appendix E, we adjusted the D&G methodology by estimating an average maximum output per extruder taking into account the evidence on factors which might affect output, such as the age of machinery and the mix of products being extruded. Secondly, we compared output per extruder in 2006 during the peak of the demand,⁵⁷ when we assumed that manufacturers were operating at close to capacity, with output per extruder in 2010. These methods suggested industry-wide spare capacity of approximately 20 per cent.
- 7.68 These robustness checks use conservative assumptions and should therefore be considered as an absolute lower bound for industry spare capacity. In contrast, our preferred method results in a reasonable point estimate, albeit one that still uses conservative assumptions. As such, the 25 per cent estimate of our preferred method and the 20 per cent lower bound indicated by the robustness checks are consistent. Calculations and assumptions are explained in more detail in Appendix E.
- 7.69 It is not possible to provide a definitive calculation of spare capacity in the market. In assessing the estimates from D&G and reaching our own estimates, we have sought to take into account constraints on apparent spare capacity and the views of the parties' competitors. Our preferred estimate indicates that industry spare capacity is, on conservative assumptions, around 25 per cent, equivalent to around 25,000 tonnes of spare capacity, with approximately 12,000 tonnes of spare capacity attributable to the merging parties and 13,000 to their competitors. We verified this estimate by other approaches.

8. Assessment of the competitive effects of the merger

- 8.1 In paragraph 6.25, we concluded that, in the absence of the merger with Epwin, Latium would have been sold to a third party, most likely another company already extruding PVC. The benchmark against which we assessed the effects of the merger was Latium remaining as an independent competitor to Epwin. In this section, we consider competition post-merger against this counterfactual and the constraint we anticipate from the merged parties' competitors for the supply of PVC roofline and window-trim products.
- 8.2 Our primary focus is whether post-merger the number of competitors would be reduced to the extent that the parties would have the ability and incentive to increase

⁵⁶ These methods did not enable us to estimate the capacity utilization rates of individual manufacturers.

⁵⁷ This assumption is supported by evidence from manufacturers which have indicated that they were operating at close to capacity during the peak of demand for PVC roofline products. D&G Consulting's industry reports suggest that demand peaked in 2006.

prices or reduce the quality or choice of their products and services to one or both of the two customer segments we have identified. In doing so, we considered specifically the implications for competition in the market of our assessment of spare capacity before examining the potential for swing capacity and other forms of market entry and expansion as potential additional sources of competitive constraint on the parties.

- 8.3 We have taken into account the potential differences depending on the type of end-user and the route to market. We initially considered separately the potential impact of the merger on the two customer segments. This is because the options of the two segments differ post-merger. We then took into account these separate analyses of the potential consequences of the merger for the market as a whole.
- 8.4 National house builders have particular requirements for distribution and product range that may preclude supply by smaller manufacturers. Pre-merger there were four suppliers to the 15 largest UK national house builders and these four options reduced to three post-merger.
- 8.5 The effect of the merger on the options of independent stockists may be different. Independent stockists may be concerned that they could only be supplied by non-vertically-integrated manufacturers, so the merger, making one non-vertically-integrated manufacturer partially vertically integrated (Latium), would remove one of their key options. Thus we analyse in more depth what sourcing options independent stockists would have post-merger in the light of our estimates on spare capacity.
- 8.6 Finally, we also consider specific submissions from third parties, highlighting what, in their view, are potential effects of the merger arising from its vertical element; that is, the fact that the merger was between one partially integrated manufacturer and one non-integrated manufacturer. Specifically, we examine the potential impact on independent stockists of post-merger multi-branding and the link between the specification and trade segments. We also look at the geographical distribution of stockists and any potential for the merged parties to foreclose independent stockists.

Potential effects on the specification segment

- 8.7 The largest house builders purchase about 300 to 500 tonnes of roofline and window-trim products each year.⁵⁸ These figures suggest that, adopting our conservative estimate of spare capacity, none of the actual and potential suppliers of the largest national house builders would be capacity constrained in supplying to these customers. We estimate that two current suppliers to the specification segment, Freefoam and Eurocell, have spare capacity between them of around 6,200 tonnes a year (see Table 4). House builders also cited two other potential suppliers, Homeline/GAP and FloPlast,⁵⁹ which each have around 1,000 to 2,000 tonnes of spare capacity.
- 8.8 Thus we conclude that each of the four alternative (two actual and two potential) suppliers to the merged parties has sufficient spare capacity to serve at least three of the large national house builders. Between them, they have sufficient spare capacity such that they could serve all top ten national house builders, were these customers

⁵⁸ Bellway, the fourth largest national house builder, told us it purchased about 300 tonnes of PVC roofline and window-trim products a year. Taylor Wimpey told us that it spent around £1 million on these PVC products. Based on a price per tonne of around £1,900–£2,000, this suggests that it is purchasing around 500 tonnes a year.

⁵⁹ We note that FloPlast told us that it did not see itself as a competitor to the larger manufacturers in the supply of PVC roofline products directly to large national house builders.

to switch away from Epwin/Latium. Therefore, in our view, customers in the specification segment would have viable alternative options to the merged parties which would constrain the merged parties' ability to increase prices or reduce quality to this segment.

Potential effects on the trade segment

- 8.9 We focused on independent stockists as some manufacturers sell part of their output through their own in-house stockists. After the merger, there were only two large non-integrated manufacturers, Freefoam and FloPlast, which did not have their own stockists through which to distribute their products and supply to a network of independent stockists. This potentially reduced the options of independent stockists.⁶⁰
- 8.10 The evidence indicated that all vertically-integrated manufacturers also sell to independent stockists. Most significantly, Epwin supplies [80–90] per cent of its PVC roofline and window trims through independent stockists and the remainder through its 43 own stockists. Given that Latium does not have any of its own stockists, the merged company is likely to sell a higher proportion of its output through independent stockists compared with the proportion Epwin sells now.
- 8.11 Other vertically integrated manufacturers also supply independent stockists. For example, Eurocell has 126 stockists but supplies independent stockists with its Deeplas brand. Similarly, Homeline/GAP is the sole supplier of cellular PVC roofline [☒] to DGS, an independent stockist network. Kalsi, a smaller manufacturer, is also partially vertically integrated, but sells around 85 per cent of its output through independent stockists.
- 8.12 For smaller independent stockists, there would appear to be a number of alternative suppliers post-merger. Most stockists are relatively small,⁶¹ and our estimates of spare capacity suggest that, in addition to the five largest manufacturers post-merger, there would be at least a further four manufacturers with spare capacity to supply independent stockists. Our survey also found that smaller stockists source from a wide variety of manufacturers and not just the largest. For example, when asked which suppliers they would consider other than their current supplier, 40 per cent did not cite one of the six largest manufacturers before the merger, suggesting that they were considering smaller manufacturers.⁶²
- 8.13 The effect of the merger may be more significant for larger stockists which may have fewer alternative suppliers than smaller stockists.⁶³ We therefore considered the potential implications of our capacity analysis on the largest independent stockist chain, SIG Plastics, which has an annual turnover 20 times higher than any other independent stockist we identified during our inquiry.
- 8.14 SIG told us that it did not expect any effects in the trade segment of the merger due to competition from Freefoam and FloPlast. Nevertheless, given its size and geographic reach compared with other independent stockists, we considered the potential effect of the merger on SIG's supplies in order to assess any potential adverse competitive effects of the merger on its trade customers.

⁶⁰ The remaining three large manufacturers post-merger (Epwin/Latium, Eurocell and Homeline/GAP) are partially vertically integrated.

⁶¹ 70 per cent of the independent stockists we surveyed had only one store (slide 3 of the [survey presentation](#)).

⁶² [Survey presentation](#), slide 29.

⁶³ SIG told us, for example, that it required manufacturers to be able to supply its stores across the UK and to supply a full range of products.

- 8.15 We estimated⁶⁴ SIG's annual sales at about [10,000–15,000] tonnes. SIG told us that around [20–30] per cent of its sales were to the specification segment, suggesting that around [5,000–10,000] tonnes of its sales are to the trade segment. Using conservative assumptions, and based on information provided by SIG and the parties, we estimate that Epwin and Latium supply approximately [4,500–5,500] tonnes of SIG's sales to the trade segment.⁶⁵
- 8.16 Our capacity estimates suggest that Freefoam would have about 3,400 tonnes of spare capacity while FloPlast would have about 2,200 tonnes of spare capacity, giving a total of 5,600 tonnes of spare capacity between them (see Table 4). Therefore, according to these estimates, SIG could, in theory, source all the Epwin and Latium products it currently supplies to the trade segment from its other current suppliers, Freefoam and FloPlast. This is without taking into account other potential suppliers' spare capacity, for example smaller manufacturers or integrated manufacturers, such as Eurocell or Homeline/GAP,⁶⁶ or available swing capacity from FloPlast (see paragraph 8.31).
- 8.17 In practice, the capacity for SIG to switch its supplies away from the parties is likely to be less relevant than the fact that it could use the availability of alternative sources of supply as a credible outside option in negotiations with the parties. This would constrain the parties' ability to raise prices relative to other suppliers on its sales to SIG for the trade segment.
- 8.18 Also, we note that it is not necessary for SIG to have an alternative supplier or suppliers for *all* the products it sources from Epwin and Latium. The threat that SIG would switch even a proportion of its supply to other manufacturers could be sufficient to constrain the parties. This is because while the parties might try to offset any loss of volume sales to SIG by increasing the price on the remaining sales, their ability to do so would be constrained by the extent to which they could sell at the higher price. We note that we found in paragraph 7.53 that stockists and end-users do not face significant barriers to changing supplier, and our survey suggests that demand is relatively elastic.⁶⁷

Conclusions on the effect on the trade segment

- 8.19 Our analysis demonstrates that SIG's view that there would be sufficient competition to constrain the merged parties in its supply to the trade segment is supported by the evidence. Based on our estimates of spare capacity, SIG would have an outside option for all the Epwin and Latium products it currently buys for sale to the trade segment.
- 8.20 We noted in paragraph 8.10 that smaller independent stockists buying relatively low volumes would also have a large number of alternative suppliers post-merger.

⁶⁴ SIG was unable to provide tonnage figures for its purchases of roofline and window-trim products because it tracks volume in metres. Therefore we estimated SIG's annual sales tonnage based on their values and average prices per tonne.

⁶⁵ SIG told us that, of its supplies to the specification segment, around [5–15] per cent was supplied by Freefoam and around [85–95] per cent by Epwin and Latium. Using a more conservative figure of [85–95] per cent supplied by Epwin and Latium gives us an estimated split of the parties' sales to SIG of around [0–5,000] tonnes to the specification segment. Given Epwin and Latium's total supply to SIG, estimated at [5,000–10,000] tonnes, this indicates the parties supply [4,500–5,500] tonnes of SIG's sales to the trade segment.

⁶⁶ There is evidence that these manufacturers sell some of their production to independent stockists. However, SIG told us that it considered Gap/Homeline and Eurocell to be competitors and [redacted].

⁶⁷ 77 per cent of installers and 81 per cent of stockists said that they would be quite likely or very likely to change supplier if the parties increased their prices by 10 per cent relative to their competitors (Figure 6.6 of the [Survey Report](#)).

- 8.21 We conclude therefore that post-merger Epwin and Latium would not have the ability to increase prices or reduce quality to the trade segment.

Summary of assessment of the implications of our spare capacity estimates

- 8.22 In paragraphs 8.7 and 8.8 we described the potential for competitors to the non-merging parties to supply from their spare capacity each of the largest ten customers in the specification segment. In paragraphs 8.9 to 8.21 we described the significant number of alternative suppliers with spare capacity for small stockists and the potential, post-merger, for larger competitors to the parties to supply from their spare capacity all the trade customers of the largest stockist.
- 8.23 Our estimate of the spare capacity of the merged parties' competitors would not be sufficient to meet demand in the unlikely scenario that all Epwin/Latium's customers across both segments wanted to change supplier simultaneously. However, in a bargaining framework, prices are constrained by a customer's ability to negotiate and to have a viable outside option as the basis for the negotiations. Not all customers of the merged parties would need to change supplier; they would need to have a viable outside option to which they could threaten to switch in negotiations. We considered that our estimate of spare capacity is such that there would be sufficient outside options across both customer segments to constrain the merged parties.

Market entry/expansion

- 8.24 As part of our overall analysis, we looked at the potential for different kinds of entry and expansion into the market to increase available capacity. We summarize the evidence below. In doing so, we note that we have concluded in paragraph 8.23 that there is sufficient spare capacity among the parties' competitors to constrain the parties post-merger.

Swing capacity

- 8.25 We noted in paragraphs 5.34 and 5.35 that the production assets used to manufacture other PVC extruded products, such as rainwater products, are similar to those used to produce roofline and window-trim products. We considered the potential for existing manufacturers of roofline and window-trim products to expand their production by reallocating production lines currently used to produce other PVC extruded products outside the market, such as rainwater products. We term this reallocation of production assets 'swing capacity'.

Views of the parties

- 8.26 As we noted in paragraph 5.23, the parties argued that manufacturers could switch easily between production of roofline and window-trim products and other PVC-extruded products. They further submitted that the same extruder can often be used to produce a variety of roofline, window and rainwater products. They also told us that an existing manufacturer of roofline and window-trim products and other PVC extruded products would incur no material additional costs from switching manufacturing between the two types of products.

Third party views

- 8.27 Of the parties' main competitors for PVC roofline and window-trim products, Freefoam, FloPlast and Kalsi also produce rainwater products. Freefoam estimated

its spare rainwater product capacity at 40 per cent but told us that it did 'not have the ability to switch from selling one class of products to another exclusively'. It did not consider that it had swing capacity beyond a base level of 5 per cent. Freefoam also said that the mix of raw materials was different for the two products and it was not necessarily possible to use the same extruder. Kalsi did not indicate that it had any swing capacity. It said that it had not switched production between products on the same line.

- 8.28 [A manufacturer] told us that it would be relatively easy to switch between rainwater and roofline. [It] told us that it supplied approximately 6,000 tonnes of rainwater products and 4,000 tonnes of other PVC building products to the UK market in 2011. It estimated its overall spare capacity at around 30 per cent. This suggests that [it] could manufacture more than our estimated 2,200 tonnes of spare capacity by using swing capacity from its rainwater extruders.
- 8.29 Other manufacturers currently outside the market for PVC roofline and window trims also noted that there were no technological barriers to switching capacity from other PVC products to roofline and window trims. For example, both [X] and [X] told us that it would be 'relatively easy' to enter the market by switching production to roofline and window-trim products. Similarly, [X], which produces roofline and window-trim products but not rainwater products, noted that the technology was the same. We consider potential entry by manufacturers of other PVC building products in paragraphs 8.34 and 8.35 below.

Our assessment of swing capacity

- 8.30 Third parties largely confirmed the view of the parties that the production processes for other PVC extruded products, and PVC roofline and window-trim products, are very similar. One of the three manufacturers currently producing both types of PVC products also told us that it would be relatively easy to use capacity from rainwater goods to expand its supply of PVC roofline and window-trim products. The other two did not currently switch capacity between the two types of products and one of these highlighted differences in the production process. Our evidence showed that there were not significant technological barriers for manufacturers of both types of product to swing capacity from other PVC extruded products to roofline and window-trim products.
- 8.31 Our view is therefore that swing capacity available to manufacturers within the market may be expected to act as a further competitive constraint on the parties. We would generally expect this swing capacity to be used only after any existing spare capacity had been exhausted. This is because spare capacity is more immediately and easily available as its use only requires running production lines longer or more efficiently. It thus provides a more timely competitive constraint than swing capacity, which is available less immediately and the use of which may require some additional costs, such as alternative tooling and downstream equipment.⁶⁸

Other forms of entry and expansion

- 8.32 We found that spare capacity in the market would place sufficient competitive constraint on the merged parties, and that the availability of swing capacity to some manufacturers in the market would also constrain the parties. We now consider the

⁶⁸ We acknowledge that in some cases, such as where the necessary capital equipment already exists, swing capacity may be readily available.

potential for other forms of entry, noting that in any event there are sufficient constraints from within the market to counteract any loss of competition brought about by the merger.

Entry by other PVC extrusion manufacturers

- 8.33 The parties told us that, in their view, entry costs were low for PVC extrusion manufacturers outside the market. Alternative tools needed to produce different types of roofline and window-trim products were readily available and were low cost on the second-hand market. For an existing manufacturer of PVC-extruded products, the parties estimated the costs of an entry level cellular product range at £200,000 using second-hand equipment and £320,000 for new equipment.
- 8.34 As we noted in paragraph 8.29, [X] and [Y] both said that it would be relatively easy to start supplying PVC roofline and window-trim products, but neither considered it to be attractive to do so. [X] told us that the ‘high volume, low margin commodity market [was] not part of our business model’.
- 8.35 The evidence indicated that the main barrier to entry to the roofline and window-trim market for manufacturers of other PVC-extruded products would be the costs of additional tooling and downstream equipment. Evidence from third parties suggested that the parties’ estimate of this cost at up to £300,000 for a small range of cellular roofline products was reasonable.

New entry

- 8.36 None of those who made submissions to our inquiry considered that the conditions were suitable to enable a new entrant to enter the market for PVC roofline and window-trim products without an existing PVC extrusion manufacturing base. Third parties variously pointed to low margins within the industry and the relatively high costs of setting up a new manufacturing facility. GAP estimated the minimum investment required for a full-scale new entrant to the market to be around £10 million. Kalsi also told us that the cost to invest in new equipment to give the quality and capacity that it had in 2012 would be around £10 million.

Entry from imports

- 8.37 The parties argued that there was potential for entry into the UK market from manufacturers of PVC roofline and window-trim products in the Republic of Ireland and mainland Europe. Some foreign manufacturers have entered the UK market. For example, FloPlast is a related company of Cork Plastics in the Republic of Ireland and distributes Cork Plastics’ products to UK stockists from a distribution base in Sittingbourne, Kent. Similarly, Plastivan UK is a distributor to UK stockists from its base in Bristol. Plastivan UK told us that it sourced approximately two-thirds of its roofline and window-trim products from its parent company, which had a manufacturing base in Belgium.
- 8.38 Both FloPlast and Plastivan UK supply from UK distribution bases. We did not examine in detail the costs associated with setting up a UK distribution base. We note that Latium told us that to set up a new warehouse and transfer out of its logistics arrangements with Trentham would take around [X] months and cost £[X] in set-up costs.
- 8.39 Others told us that there were barriers to foreign companies trying to export to the UK. Freefoam told us that it was not particularly easy to import roofline and window-

trim products from the Republic of Ireland or mainland Europe for distribution in the UK. Its own experience had been that it was more cost-effective to set up a UK production facility than to import from the Republic of Ireland as it had done until 2006. This was because of currency risks and the fact that cellular roofline was a bulky product and therefore expensive to transport.

Expansion

- 8.40 The parties' competitors told us that expanding their existing capacity would be costly and take time and hence would not be justified in current market conditions with low margins and excess capacity. For example, Eurocell, Freefoam, Kalsi and Gap/Homeline provided estimates ranging from around £0.25 million to £0.5 million for a new fully-functioning extrusion line, and estimated the time to get new equipment running at full capacity from a few months to a year. Third parties suggested that while it would take time to implement a new product range with new tools and other equipment, estimates suggested months rather than years.

Our assessment of other forms of entry and expansion

- 8.41 The evidence we have received suggested that there was little immediate prospect of entry into the market by companies outside the market producing related PVC-extruded products, or for expansion by those already in the market. This was consistent with the evidence we received that the UK PVC roofline and window-trim market is one of low margins and existing spare capacity.
- 8.42 The main barrier to entry or expansion from those within the PVC extrusion industry in the UK appears to be the low return on the capital investment required. We note estimates of the costs of various types of entry and expansion from third parties from around £0.25 million upwards. Those importing from abroad may face additional barriers in the form of transportation costs and currency risk.
- 8.43 The evidence we considered suggested that entry by an existing manufacturer of PVC building products, with access to raw materials at competitive prices, could be achieved for a relatively modest investment in time and money and also that there was potential for increased imports if exchange rates were favourable. Either of these could provide a constraint on the merged entity if market conditions changed. There was a general consensus that the barriers were high for a party to enter the PVC roofline and window-trim market from outside the PVC extrusion industry.

Countervailing buyer power

- 8.44 The Guidelines state that the existence of countervailing buyer power will be a factor in making an SLC finding less likely.⁶⁹ They describe circumstances where 'an individual customer may be able to use its negotiating strength to limit the ability of a merged firm to raise prices'.⁷⁰ As we noted in paragraphs 7.11 to 7.14, those buying from manufacturers (national house builders and stockists) frequently negotiate prices in what we characterize as a bargaining framework. In such a framework, where buyers have a good alternative option, their negotiating position is strong. Our analysis of spare capacity in paragraphs 7.55 to 7.69, swing capacity in paragraphs 8.25 to 8.31 and switching costs in paragraphs 7.38 to 7.54 demonstrated that

⁶⁹ The Guidelines, paragraph 5.9.1.

⁷⁰ *ibid.*

national house builders and stockists have credible alternative options and as such we would expect them to have a degree of buyer power. We also note that all the national house builders which responded to our questionnaire considered that they either had buyer power or that they were able to use the volumes they purchased to help them negotiate lower prices.

The potential effect of the merger on the distribution of PVC roofline and window-trim products

8.45 The merger in this case is between two companies at the same level in the supply chain, and our analysis concentrated on what we considered to be the most likely horizontal effects of the merger. However, some competitors and stockists have argued that there were potential anti-competitive effects from the vertical element of the merger. The vertical element arose from the fact that one of the non-integrated manufacturers (Latium) would post-merger have access to the integrated stockists of Epwin. It was suggested to us that the merged entity would be able to exert pressure on the way products are distributed with results that would be anti-competitive. We deal with the specific submissions made below.

Post-merger multi-branding

8.46 Freefoam told us that Epwin would be able to use the seven roofline brands available to it post-merger (its own four main brands plus Latium's three) to offer geographic exclusivity to independent stockists. This would be to the detriment of manufacturers with one brand who could not offer neighbouring stockists brand exclusivity. Freefoam told us that it had decided not to adopt a multi-brand strategy because it would dilute the value of its brand.

8.47 There was limited evidence that stockists request geographic brand exclusivity. We did receive evidence that some stockists buy stock from more than one manufacturer. Two of the eight large stockists from which we received responses bought stock from more than one manufacturer. Also, of the Epwin and Latium stockists we surveyed that typically ask for a brand, 25 per cent asked for brands of other manufacturers, suggesting that they multi-source. Epwin told us that it did not offer exclusive agreements in which it sold particular brands to individual stockists. We noted in paragraph 7.28 that our survey evidence suggested that brand was not an important factor for installers.

Our assessment

8.48 We did not consider this issue to raise competition concerns for two main reasons. First, both Epwin and Latium had multiple brands in their portfolio prior to the merger. Therefore, the suggested strategic effect of branding would only arise as a result of this merger if there were at least four independent stockists selling Epwin or Latium products in the same catchment areas and all required brand exclusivity. This is because Epwin had three main brands it sold to the trade segment pre-merger and would therefore have been able to offer exclusive supply of one brand to up to three independent stockists. The merger cannot be expected to have a detrimental effect on independent stockists unless at least four such stockists were seeking exclusive brands in the same locality and we do not expect that to be the case.⁷¹

⁷¹ See distribution of stockists in Appendix F.

- 8.49 Second, while we accept that there may be costs involved in establishing a new brand, it is open to the parties' competitors to do so. Freefoam told us that it chose to adopt a single-brand strategy. We assumed therefore that this choice was based on an analysis of its costs and benefits compared with the alternative of a multi-brand strategy. We therefore consider that the merger of two companies with multiple brands does not raise competition concerns.

Link between specification and trade segments

- 8.50 The second issue concerned the potential ability of the merged parties to entice a stockist to switch to them by offering new business from the specification sector. This potential, it was suggested to us, would increase post-merger because of the parties' strong position in the specification segment.
- 8.51 Stockists told us that specification agreements usually give them lower margins compared with sales to the trade segments. Thus, even though they generate additional revenues, it is not clear that they are attractive to all stockists because of the potential to take shelf space from higher margin sales. Epwin told us that some stockists prefer to avoid participating in the specification segment and there was some support for this view from third parties.⁷² This evidence indicated that the merger is unlikely to result in the merged parties having the ability to encourage stockists to switch supplier in return for increased sales into the specification segment.

Foreclosure of independent stockists

- 8.52 We were told that one potential effect of the merger was that the merged parties could threaten to withdraw a brand or product from independent stockists in favour of their own outlets if the stockist did not accept margin arrangements agreed with end-users in the specification segment. It was argued that this potential foreclosure of independent stockists could lead to them going out of business which would reduce the routes to market for non-integrated manufacturers and therefore the choice to end-users.
- 8.53 In order to foreclose independent stockists, the merged parties would need to have sufficient outlets of their own to supply end-users. Epwin has 27 plastics stockists and 16 Windowstore outlets which primarily stock windows and doors but also sell roofline products. To understand further the geographic coverage of this distribution network compared with other integrated stockists and independent stockists, we created a series of UK maps. These plot each stockist and 10-mile radii around the centre to represent graphically an approximate catchment area of an individual stockist.⁷³
- 8.54 Not all independent stockists are plotted on these maps. We had contact details for 1,151 non-integrated stockists supplied by Epwin and Latium and 177 of the 199 SIG stores.⁷⁴ The plotted integrated stockists for the other distribution networks mapped should be complete. The maps and a brief description of what they show are in Appendix F.

⁷² For example, [a major stockist] told us that cellular margins had consistently tightened over the past few years and were only attractive to it if additional products could be sold to the house builder or larger contractor. It also said that it might choose not to participate if the margin generated was not sufficient to cover its distribution costs and liabilities. [§<], another stockist chain, said that it had been involved in these arrangements previously but found the lack of control over its margin unacceptable.

⁷³ DGS told us that customers generally travelled no more than 10 miles to a stockist.

⁷⁴ We note the OFT's estimate of 4,000 to 5,000 outlets for PVC building products.

- 8.55 The maps suggest that Epwin's ability to foreclose independent stockists would be restricted by the limited scope of its distribution network. With only 43 outlets, we consider it unlikely that it would have the ability or incentive to foreclose independent stockists.
- 8.56 We also note that in paragraph 8.12, our view was that independent stockists would have an outside option to the merged parties because there were a large number of alternative suppliers with spare capacity. We further noted in paragraph 7.54 that in our view there were no significant switching costs for stockists.
- 8.57 We therefore consider that it is not likely that the merged parties would be able to foreclose independent stockists.

Conclusions on the assessment of the competitive effects of the merger

- 8.58 The main focus of our analysis was on the unilateral horizontal effects of the merger between Epwin and Latium. That is, we considered the potential that the removal of the competitive constraint provided by each party to the other pre-merger would enable the merged company to raise prices profitably or reduce quality or choice without needing to coordinate with its rivals. Based on our conclusion on the counter-factual that in the absence of the merger Latium would have been purchased by another third party, we analysed the competitive effects of the merger compared with the benchmark that Latium would have remained an independent competitor to Epwin.
- 8.59 Our analysis led us to conclude that the UK market for PVC roofline and window-trim products is characterized by a bargaining framework in which prices are decided following bilateral negotiations. We considered that in such a market the outside option of end-users is determined by the extent to which the products are homogeneous, the existence and scale of any switching costs and the extent to which alternative sources of supply are capacity constrained.
- 8.60 Our view was that the products were broadly homogeneous and that switching costs were not of a magnitude to prevent end-users changing supplier to meet their requirements. We conservatively estimated spare capacity in the industry at around 25 per cent. Our view was that, based on this estimate of spare capacity, there would be sufficient available alternatives for each of the customer segments we identified such that the parties' ability to raise prices profitably or reduce quality or choice would be constrained.
- 8.61 We considered that swing capacity available to manufacturers in the market which also produce PVC-extruded products would also constrain the parties.
- 8.62 We note that the evidence we have received suggests that barriers to entry and expansion from other PVC manufacturers in the UK and Europe are mainly related to the capital investment required which appears relatively modest. However, we further note that entry or expansion is unlikely given current market conditions because of low margins and spare capacity.
- 8.63 We noted that, for both the trade and specification segments, prices are typically negotiated bilaterally between customers and manufacturers or stockists. Our assessment on switching shows that customers in both segments have the ability to threaten to switch to credible alternative manufacturers with relative ease. Therefore, we consider that customers in both segments of the market have the ability to negotiate.

8.64 We also considered potential non-horizontal effects of the merger in the light of submissions from third parties. We find that there are no competition concerns arising from the portfolio of brands available to the merged parties. The evidence indicates that the merged parties would not be able to offer business in the specification segment as an incentive to encourage independent stockists to switch to them. Also, we consider that the parties would not have the ability to foreclose independent stockists.

Conclusions on the SLC test

8.65 We conclude that the merger has not resulted, and may not be expected to result, in an SLC within any market or markets in the UK for goods or services.